

COMMENTS

INVESTMENT IN THE PEOPLE'S REPUBLIC OF CHINA: THE BASIC LEGAL FRAMEWORK

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1. INTRODUCTION

Doing business in or with the People's Republic of China (P.R.C.) has gained in popularity in recent years. Statistics show that the number of representative offices of foreign businesses has increased from year to year, and by September 1988, there were already 1,047 foreign representative offices in Beijing.¹ "This signifies," according to the Xinghua News Agency, "that the interests of foreign countries in developing trade with, and expanding investment in, China have never been changed."² Foreign investment in the P.R.C. has increased significantly over the years,³ and the P.R.C.'s foreign trade has more than doubled in the last decade.⁴ According to one source, the P.R.C.'s exports in 1987 totalled 34.6 billion dollars, 256% higher than that in 1978. Similarly, its imports in 1987 totalled 33.4 billion dollars, 210% higher than that in 1978.⁵ At the same time, the P.R.C.'s legal system,

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The author is grateful to Professor Soltysinski for his invaluable supervision and comments on the drafts of this article. Thanks also go to the author's classmates who shared with him the enjoyment of a wonderful seminar on Legal Problems of East-West Trade conducted by Professor Soltysinski at the University of Pennsylvania. Of course, all mistakes herein bear the sole name of the author himself.

1. *See The Number of Foreign Enterprise Representative Offices in Beijing Over 1000*. People's Daily, Sept. 23, 1988, at 1.

2. *Id.*

3. *See infra* notes 14 - 16 and accompanying text.

4. *See China's Foreign Trade More Than Doubled in Ten Years*, Renmin Ribao (Hawaii Ban) (People's Daily (overseas ed.)) [hereinafter People's Daily], Aug. 20, 1988, at 1.

5. *Id.*

which is directed towards the realization of its "four socialist modernizations," has been under dramatic development, especially in the regulation of foreign economic transactions.⁶ The first section of this paper describes the achievements the Chinese have made during the past decade in foreign economic transactions and their underlying policy considerations and regulations. A brief comparison of the P.R.C. with other socialist countries is also presented. The second, third and fourth sections describe the general characteristics of applicable Chinese laws, the regulatory framework at various levels, and the foreign trade transactions chain involving foreign trade organizations (FTO's) and other partners. The fifth section discusses the forms of foreign investment currently available in the P.R.C. for foreign investors and the basic legal provisions and practices which relate to them. The remaining sections deal with special issues foreign investors may encounter, such as starting procedures, managerial and operational matters, technology transfer, taxation, financing and foreign exchange regulations, and dispute resolution. Other equally important issues such as contract formation, investment protection, and import-export and domestic sales are not addressed in this article. This study is not intended to be a comprehensive treatment of the laws and practices governing foreign investment in the P.R.C. As the title suggests, this article only provides a description and an analysis of the basic legal framework for foreign investment in the P.R.C.

2. 1978-1988: A DECADE OF DEVELOPMENT

2.1. *A Decade of Development*

Since the Third Plenary Session of the Eleventh Central Committee of the Communist Party of China in 1978, when it first began to open its doors to the outside world, the P.R.C. has been actively and successfully absorbing and utilizing foreign investment. The scale has been extensively expanded and a "new structure of foreign investment utilization" is being formed from coastal and limited areas to inland and larger areas throughout the P.R.C.⁷ The former "closed or semi-closed" economy is becoming a more open one, as evidenced by the nation's increasingly active economic and technical intercourse and co-

6. The "four modernizations" consist of industrial modernization, agricultural modernization, national defense modernization, and science and technology modernization.

7. See *Benefits From Foreign Investment Utilization in China Becoming More and More Obvious*, People's Daily, Sept. 10, 1987, at 1 [hereinafter *Foreign Investment Utilization*].

operation with foreign countries. In order to carry out its open-door policy, the P.R.C. established four special economic zones (SEZs) in Guangdong and Fujian Provinces,⁸ 14 coastal open cities,⁹ and certain inland cities,¹⁰ and, more importantly, enacted laws and regulations in the area of economic (particularly foreign economic) relations. Since 1979 there have been more than 500 laws and regulations enacted or promulgated by the national legislative and semi-legislative bodies. Over 350 of these are economic (including foreign economic) laws and regulations, more than 260 of which deal directly with or affect the P.R.C.'s foreign business transactions.¹¹ During the same period, more than 1,000 pieces of local legislation were promulgated, of which over 300 regulate domestic and foreign economic transactions.¹²

The development of the nation's open-door policy and its legal system has substantially improved the P.R.C.'s foreign investment environment and increased its attractiveness to foreign investors. As the People's Daily reports, the P.R.C.'s emerging foreign economic legal system has functioned favorably in absorbing foreign investment and improving the P.R.C.'s investment atmosphere. As of the end of June

8. The four special economic zones are: Shenzhen, Zhuhai, Shantou (Guangdong Province), and Xiamen (Fujian Province). The SEZ's are designed to develop economic cooperation, to realize significant economic benefits, to encourage foreign investment and promote trade, to introduce foreign technology, know-how and management techniques to other parts of the P.R.C., and to serve as centers for education and experimentation. See Xu, *China's Special Economic Zones*, BEIJING REV., Dec. 14, 1981, at 14-15. The designation of Shanlou, Shenzhen, and Zhuhai as SEZ's took place in August 1980. NPC Approved Regulations on Guangdong Special Economic Zones, CHINA ECON. NEWS, Sept. 1, 1980, at 2. The Huli SEZ in Xiamen was announced in October 1980. See INVESTMENT GUIDE TO XIAMEN SPECIAL ECONOMIC ZONE (Hong Kong, 1984). In March 1984, however, the entire city of Xiamen, covering an area of 131 square kilometers with a population of 350,000, was declared a SEZ. See *Changes in Xiamen Zone*, BUS. CHINA, Nov. 14, 1984, at 163.

9. The 14 Coastal Open Cities are, from south to north: Beihai, Zhanjiang, Guangzhou, Fuzhou, Wenzhou, Ningbo, Shanghai, Nantong, Lianyungang, Qingdao, Yantai, Qinhuangdao, Tianjin, and Dalian. On March 15, 1984, the date on which the Xiamen SEZ was expanded, Premier Zhao Ziyang announced that certain cities along the coast would be selected for a special program analogous to that of the SEZs. The policies of the program focus on two major points, increased preferential tax treatment and increased access to the domestic market for foreign investors, and an expansion of the decision-making powers of local authorities participating in economic and technical co-operation projects with foreigners. In November 1984, the State Council issued Provisional Regulations on tax reduction and exemption in both the SEZs and the 14 coastal open cities. See Tay, *infra* note 85.

10. The inland cities include Beijing, Chongqing, Shenyang, Wuhan, and Xi'an. See People's Daily, Oct. 13, 1987, at 3. Note that a larger and "more special" SEZ has come onto the scene - Hainan Island - which has been upgraded to the status of a "Province." See *infra* notes 65-67 and accompanying text.

11. See *China's Foreign Economic Law and Regulation System is Formed*, People's Daily, Nov. 11, 1988, at 3.

12. See People's Daily, Oct. 12, 1987, at 4.

1987, each province, municipality and autonomous region on the mainland, with the exception of Tibet, has established economic relations with, and benefited from direct and indirect investments from foreign business entities.¹³

According to statistics recently released by the State Bureau of Statistics, over 10,000 contracts and agreements totalling \$62.5 billion dollars have been negotiated and finalized between Chinese and foreign investors since 1979. Of this amount, \$37.5 billion (60% of the total investment) has been channelled into actual use over the last ten years.¹⁴ The primary portion of the contractual investment amount (71.5% of the total) was contracted in the form of low to medium-low interest or even interest-free foreign loans, mostly on a long-term basis. The second largest portion (22.8% of the total) has been in the form of direct foreign investments in joint ventures and wholly foreign-owned ventures in the P.R.C. The remaining portion of the contractual investment amount (5.7% of the total) was contracted in forms such as compensation trade, processing and assembling transactions and international leases.¹⁵

The development of foreign investment in the P.R.C. is also apparent from the broad geographical representation of foreign partners. In 1979, only twenty states and regions were involved in providing loans and engaged in investment activity in the P.R.C. Today, there are hundreds of foreign entities and individuals investing in the P.R.C., representing over forty countries and regions.¹⁶

2.2. *The Nature and Role of Foreign Investment in China*

There are at least three reasons for the P.R.C. to encourage and utilize foreign investments on a large scale. First, the use of foreign investment allows it to replenish the supply of capital necessary for the construction and development of "socialist modernizations." Second, such use will allow the P.R.C. to more effectively introduce sophisticated equipment and technology as well as advanced management techniques from other countries. Third, it will allow for the promotion and expansion of the P.R.C.'s export capacity.¹⁷

13. *Foreign Investment Utilization*, *supra* note 7.

14. *Scale of China's Use of Foreign Investment Further Expanded*, People's Daily, Oct. 21, 1988, at 1 [hereinafter *Foreign Investment Use Expanded*].

15. *Id.* Guangdong and Fujian remain the most influential provinces in absorbing and utilizing foreign investments, either direct or indirect. These two regions alone contracted some \$12.62 billion with foreign investors and banking institutions from 1979 to 1987. Of this figure, \$4.85 billion has been put to full use. *Id.*

16. *Id.* The term "regions" denote areas such as Hong Kong and Macao.

17. Most of the foreign-invested enterprises in the P.R.C. are export-oriented.

The nature of Chinese socialism will not be affected by the fact that a substantial portion of the P.R.C.'s economy could take the form of joint venture production (equity or non-equity), wholly foreign-owned enterprises, or the P.R.C.'s own private economy. On the contrary, in general the P.R.C.'s economic force firmly adheres to state-owned and collectively-owned enterprises.¹⁸ It should be borne in mind that, being a developing socialist country under a planned economy, the P.R.C. must direct any new legislation toward serving and accommodating its economic system and structure.¹⁹ Allowing foreign investment will inevitably change the means by which the P.R.C. will achieve the ultimate goal of the "socialist modernizations." Already, capitalist skills, methods and philosophy of management introduced by foreign investors has been and will continue to influence the conduct of many state enterprises. The 1982 Constitution of the P.R.C. treats the individual economy (*geti jingji*) or the private enterprises (*siren qiye*) operating within the limits prescribed by law as a complement to the State's socialist economy of public ownership.²⁰ Article 18 of the Constitution mandates that the law of the P.R.C. permit foreign investment therein, that all P.R.C.-based foreign enterprises, foreign economic institutions, Chinese-foreign joint ventures, and their lawful rights and interests be protected so long as they abide by the P.R.C.'s laws and regulations.²¹

2.3. *China and Other Socialist Countries*

Foreign investment and the joint venture are not new phenomena to socialist countries.²² Yugoslavia, Hungary and Romania have all

To the author's understanding, one of the major policy considerations underlying the absorption of foreign investment is to increase the nation's overall capacity and to earn much needed foreign exchange.

18. See the Constitution of the People's Republic of China of 1982 [hereinafter cited as Constitution of the P.R.C.], Art. 6, *reprinted and translated in* 1 CCH CHINA LAWS FOR FOREIGN BUSINESS (CCH Australia Ltd., 1987 ed.) ¶4-500 [hereinafter CCH CHINA LAWS].

19. See Horsley, *Comments on Laws and Developments Affecting Foreign Investments in China*, 3 CHINA L. REP. 175, 177 (1986) [hereinafter Horsley, *Comments on Laws and Developments*]. Foreign exchange, for example, is under centralized control in the P.R.C. If a foreigner has taken foreign currency into the P.R.C., he may take it back out with him. See Foreign Exchange Control Regulations, *infra* note 55, art. 18. However, if a foreign enterprise has deposited foreign currency into the Bank of China, it must apply to the Bank in order to withdraw and remit a specified sum out of China. The P.R.C.'s Foreign Exchange Control Regulations provide that any "legitimate profits and other legitimate earnings" of foreign enterprises may be remitted. *Id.*, art. 24.

20. Constitution of the P.R.C., *supra* note 18, art. 11.

21. *Id.*, art. 18.

22. See Rich, *Joint Ventures in China: The Legal Challenge*, 15 INT'L LAW.

183, 189-90 (1981).

previously engaged in such activity.²³ What is unique to the P.R.C., however, is: 1) the number of foreign investors permitted to participate; 2) the emergence of the special economic zones; and 3) the ability of foreign partners to become 100% owners.²⁴

It is not denied that there are certain similarities between the East European socialist countries and the P.R.C. For instance, both Eastern Europe and the P.R.C. have long been isolated from the Western industrial nations. Although both the East European countries and the P.R.C. strongly wished to obtain foreign investment and to acquire advanced technology from abroad early on, this desire in both instances "was tempered by a suspicion of foreign investors."²⁵ In addition, new legislation in both Eastern Europe and the P.R.C. has been directed towards encouraging foreign investors to participate in each of these nations' economic construction and development. The P.R.C. is also said to have adopted several measures already taken by the East European countries.²⁶ The laws in those countries, however, were promulgated in the context of a sophisticated European legal tradition which is lacking in the P.R.C.

Neither the East European models nor the Soviet model²⁷ are directly followed by the Chinese. Nevertheless, there are some common experiences which have been taken into consideration. The fact that East European countries have adopted the joint venture as a vehicle for the development of foreign investment in their countries indicates that they recognized the need to introduce advanced technology and were willing to negotiate joint ventures with Western businessmen in a practical and non-dogmatic manner.²⁸ This is similar to the Chinese experience. In fact, the P.R.C. recently embarked upon legislation in the area of foreign economic and trade relations after conducting serious studies of the experiences of socialist countries such as Yugoslavia, Romania and Hungary.²⁹

23. Yugoslavia began to permit Western investment in its state-owned industrial enterprises in 1967. Romania followed suit in 1971 and Hungary, in 1972. *Id.*

24. Goldman, *Soviet Perceptions of Chinese Economic Reforms and the Implications for Reform in the U.S.S.R.*, 39 J. INT'L AFF. 41, 51-52 (1986).

25. Rich, *supra* note 22, at 190. Of course, it was the foreign investors who were considered to be "suspicious," not the host country. The Chinese were more cautious in dealing with foreigners (especially Westerners) for fear that they might do harm to the Chinese government or its people.

26. *Id.*

27. For a discussion of the foreign trade models of the Soviet Union and other socialist countries, see T. HOYA, *EAST-WEST TRADE* 11, 289 (1984).

28. See Scriven, *Joint Ventures in Poland: A Socialist Approach to Foreign Investment Legislation*, 14 J. WORLD TRADE L. 424, 437 (1980).

29. Radway, *Overview of Foreign Joint Ventures*, 38 BUS. LAW. 1040, 1045 (1983).

3. GENERAL CHARACTERISTICS OF THE APPLICABLE LAWS

Rather than immediately attempt a comprehensive codification of its laws regulating economic and commercial activity, the P.R.C. "opted for a more patient approach in promulgating guidelines for international investment."³⁰ Currently, there is no single civil or commercial code which covers all aspects of foreign trade and investment along with other aspects of commercial activities. Chinese legislation in this field is approached on a step-by-step basis and began to accelerate after the death of Mao Zedong in 1976.³¹ Today, there are more than 260 separate pieces of laws and regulations which deal with or affect foreign activities,³² of which over 100 directly pertain to the regulation of foreign transactions. These regulatory instruments constitute a substantive legal framework for the P.R.C.'s foreign trade and economic relations. Additionally, the majority of the P.R.C.'s legislative documents pertaining to foreign investment conform to international practice and custom ("The laws may be short and rather vague, but the principles enunciated are reassuring and in many cases extremely familiar to foreign investors.").³³ Thus, the lack of a comprehensive civil or commercial code does not impede the development of foreign investment in the P.R.C.

Currently, the relevant laws and regulations which pertain to the development of investment in the P.R.C. include: 1) enactments by the National People's Congress (N.P.C.) and its Standing Committee; 2) promulgations by the State Council and its related departments; 3) international conventions and agreements; and 4) provincial and municipal regulations.

3.1. *Legislation by the National People's Congress*

There is an increasing number of legislative documents as well as other forms of governing provisions which deal specifically with or directly affect foreign investments in the People's Republic of China. The most significant aspect of this entire body of law is the national legislation which has been promulgated by the National People's Congress, which functions as a legislative body along with its Standing Commit-

30. Wilson, *The Legal Structures Governing Technology Transfers and Joint Ventures with the People's Republic of China*, 3 INT'L TAX & BUS. LAW. 1, 2 (1985).

31. Chinese legislation in foreign economic relations was essentially a vacuum before 1979 when foreign trade and transactions were guided by internal policies and "guidelines." The majority of foreign economic laws were first enacted during the 1919-1988 period.

32. *Interview with Gu Ming*, People's Daily, Oct. 30, 1987, at 3.

33. Horsley, *Comments on Laws and Developments*, *supra* note 19, at 179.

tee.³⁴ Legislation by the N.P.C. usually results in regulations appearing in the form of "Law" (*fa*). Three important pieces of basic legislation promulgated by the N.P.C. concerning foreign investment in the P.R.C. are the Sino-Foreign Joint Venture Law of 1979, the Wholly Foreign-Owned Enterprise Law of 1986, and the Sino-Foreign Co-Operative Enterprise Law of 1988.³⁵

The adoption and promulgation of the Joint Venture Law in 1979,³⁶ which sketches the fundamental legal aspects of joint ventures, marked the beginning of a series of legislative and administrative efforts to develop a legal framework for foreign investments in the P.R.C. The Joint Venture Law officially declared to the outside world that the P.R.C. was ready and willing to pursue an open-door policy, and was prepared to welcome and encourage foreign governments, enterprises, individuals, and international institutions to invest in the P.R.C. On the other hand, the Wholly Foreign-Owned Enterprise Law of 1986³⁷ sets forth the basic framework for establishing and operating wholly foreign-owned enterprises based in the P.R.C. The Sino-Foreign Co-Operative Enterprise Law, a long-awaited piece of NPC Legislation, was finally adopted at the First Session of the Seventh National People's Congress on April 13, 1988. It gives a clear legislative framework for the formation and operation of Sino-foreign contractual joint ventures.³⁸ These three "laws" are illustrative of the typical "enabling leg-

34. See Constitution of the P.R.C., *supra* note 18, arts. 58, 62(3), 67(2).

35. The drafting of the Law of the People's Republic of China on Chinese-Foreign Co-Operative Enterprises, which began several years ago, took several years to complete. See Wei, *Further Emancipate the Mind and Create a New Situation in Absorbing Foreign Investment*, 1984 ALMANAC OF CHINA'S FOREIGN AND ECONOMIC TRADE 397 [hereinafter 1984 ALMANAC].

36. *Zhonghua Renmin Gonghe Guo Zhongwai Hezi Jingying Qiye Fa* [Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment], adopted by the National People's Congress on July 1, 1979, promulgated on July 8, 1979, reprinted and translated in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-500 [hereinafter Joint Venture Law]; 1 CHINA'S FOREIGN ECONOMIC LEGISLATION 1, 8 (1982) [hereinafter FOREIGN ECONOMIC LEGISLATION].

This law is also known as the Law of the People's Republic of China on Sino-Foreign Joint Equity Ventures. See 1 CCH CHINA LAWS, *supra* note 18, ¶ 6-500.

37. *Zhonghua Renmin Gonghe Guo Waizi Qiye Fa* [Law of the People's Republic of China Concerning Enterprises with Sole Foreign Investment], adopted by the Sixth National People's Congress on Apr. 11, 1986, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 13-506 [hereinafter Wholly Foreign-Owned Enterprise Law].

The Wholly Foreign-Owned Enterprise Law is also known as the Law of the People's Republic of China on Enterprises Operated Exclusively With Foreign Capital. See 3 STATUTES AND REGULATIONS OF THE PEOPLE'S REPUBLIC OF CHINA #860412 (1988).

38. *Zhongwai Hezuo Jingying Qiye Fa* [Law of the People's Republic of China of Sino-Foreign Co-Operative Enterprises], adopted at the First Session of the Seventh National People's Congress on Apr. 13, 1988, reprinted and translated in 1 CCH

islation" which must be accompanied by implementing and/or supplementary legislation and regulations in order to be fully effective.³⁹

The N.P.C. has produced a number of other national legislative documents in the form of "law" (statutes) which deal with or relate to foreign investments. For instance, the provisions of the Trial Civil Procedure Code of 1982 require that foreign partners basically enjoy the same rights as Chinese citizens.⁴⁰ The Economic Contract Law of 1981 is equally applicable to both Chinese economic entities and Chinese-foreign joint ventures with the latter treated as Chinese enterprises.⁴¹ The Foreign Economic Contract Law of 1985 applies to economic contracts concluded between Chinese enterprises or economic organizations and foreign enterprises, economic organizations or individuals.⁴² The General Principles of Civil Law of 1986⁴³ defines fundamental legal concepts, including the concept of "legal person," liability for certain civil actions, and the protection of intellectual property rights.⁴⁴ The Joint Venture Income Tax Law of 1980 guides the levy of or exemption from tax on income earned by the Chinese-foreign joint venture.⁴⁵

CHINA LAWS, *supra* note 18, at ¶ 6-100 [hereinafter Co-Operative Enterprise Law].

39. See Alford & Birenbaum, *Ventures in China Trade: An Analysis of China's Emerging Legal Framework for the Regulation of Foreign Investment*, 3 NW. J. INT'L L. & BUS. 56 (1981).

40. *Zhonghua Renmin Gonghe Guo Minshi Susong Fa* [Code of Civil Procedure of the People's Republic of China (Trial Implementation)], adopted by the Fifth National People's Congress on Mar. 8, 1982, effective on Oct. 1, 1982, pt. V, art. 186 ("A foreign national or stateless person who sues or is sued before a people's court shall have the same rights and obligations of litigation as a citizen of the People's Republic of China"), reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 19-200 [hereinafter Trial Civil Procedure Code].

41. *Zhonghua Renmin Gonghe Guo Jingji Hetong Fa* [Economic Contract Law of the People's Republic of China] (adopted by the Fourth Session of the Fifth National People's Congress on Dec. 13, 1988), reprinted and translated in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 5-500 [hereinafter Economic Contract Law].

42. *Zhonghua Renmin Gonghe Guo Shewai Jingji Hetong Fa* [Foreign Economic Contract Law of the People's Republic of China], adopted by the Tenth Session Standing Committee of the Sixth National People's Congress on Mar. 21, 1985, reprinted and translated in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 5-550 [hereinafter Foreign Economic Contract Law].

43. *Zhonghua Renmin Gonghe Guo Min Fa Tongze* [General Principles of Civil Law of the People's Republic of China], adopted by the Fourth National People's Congress on Apr. 12, 1986, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 19-150 [hereinafter General Principles of Civil Law].

44. The General Principles of Civil Law, however, do not specifically define what types of intellectual property rights are protected under it.

45. *Zhonghua Renmin Gonghe Guo Zhongwai Hezi Yingying Qiye Suode Shui Fa* [The Income Tax Law of the People's Republic of China Concerning Joint Ventures with Chinese and Foreign Investment], adopted at the Third Session of the Fifth National People's Congress on Sept. 10, 1980, amended on Sept. 2, 1983, reprinted & translated in 3 CCH CHINA LAWS ¶ 33-500, *supra* note 18 [hereinafter Joint Venture Income Tax Law]; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 36, 41.

Lastly, the Foreign Enterprise Income Tax Law of 1981 primarily regulates income tax matters concerning "foreign companies, enterprises and other economic organizations which have establishments in the People's Republic of China engaged in independent business operation or co-operative production or joint business operation with Chinese enterprises."⁴⁶

3.2. Regulations⁴⁷

Regulations promulgated by the N.P.C. bear the titles of "regulations" (*tiaoli*), "regulations for implementation" (*shishi tiaoli*), "provisions" (*guiding*),⁴⁸ "procedures" (*banfa*),⁴⁹ "implementing measures" (*shishi banfa*), "implementing detailed rules" or simply "rules" (*shixing xize*) and "notice" (*tongzhi*), and are the authorized productions of the State Council and its various administrative agencies. The State Council is empowered to promulgate certain regulations, provisions and procedures that are of secondary importance in relation to the "laws" enacted by the National People's Congress. The various ministries of the State Council are authorized, often subject to approval by the State Council, to formulate and promulgate "detailed rules" for implementing enactments and promulgations made by the National People's Congress, its Standing Committee, and the State Council.⁵⁰ Since 1979, numerous semi-legislative documents pertaining to or affecting foreign investments have been promulgated by the State Council and ministry-level agencies thereunder. These include the Sino-Foreign Joint Venture Registration Regulations of 1980,⁵¹ the Sino-Foreign Joint Ven-

46. *Waiguo Qiye Suode Shui Fa* [The Foreign Enterprise Income Tax Law of the People's Republic of China], enacted by the Fourth Session of the Fifth National People's Congress on Dec. 13, 1981, art. 1, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 32-500 [hereinafter Foreign Enterprise Income Tax Law]; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 64, 70.

47. It is difficult to precisely define this category. It is true that many, if not most, regulations promulgated by administrative agencies are "administrative regulations" but many are not. As Visiting Professor Soltysinski of the University of Pennsylvania School of Law commented on the draft of this article, these regulations, especially those issued by the State Council, do "create rights and obligations of civil law nature in some instances." The standard used here for differentiating "laws" and "regulations" is, however, quite simple: the National People's Congress, which is the sole State organ exercising full legislative power, passes "laws" whereas the State Council and other agencies which, though having limited quasi-legislative powers, function primarily as administrative organs and issue secondary regulations, many of which are administrative in nature.

48. *Guiding* is also translated as "regulations."

49. *Banfa* is also translated as "measures" or occasionally as "regulations."

50. See Constitution of the P.R.C., *supra* note 18, arts. 89(1), 90.

51. *Zhonghua Renmin Gonghe Guo Zhongwai Hezi Jingying Qiye Dengji Guanli Banfa* [Regulations of the People's Republic of China on the Administration of
<https://scholarship.law.upenn.edu/jil/vol10/iss3/4>

ture Implementation Regulations of 1983⁵² and the Joint Venture Labor Management Provisions of 1980, which provide guidance on labor management for joint venture operations.⁵³

Several of the administrative regulations have been issued as "interim" or "provisional" (*zanxing*) regulations. This suggests that, although presently valid and in force, these provisions are still operating on a trial basis and are likely to be subject to future modifications or amendments upon new situational developments and changes. Two examples of such promulgations are the Interim Provisions for the Control of Resident Representative Offices of Foreign Enterprises of 1980,⁵⁴ which allows foreign corporations to establish representative offices in the P.R.C., and the Provisional Regulations for Foreign Exchange Control of the People's Republic of China of 1980, which regulates foreign exchange controls relating to both Chinese economic organizations and individuals and foreign institutions in the P.R.C. (and their personnel and Chinese-foreign joint ventures and their

the Registration of Joint Ventures Using Chinese and Foreign Investment], *promulgated* by the State Council on June 26, 1980, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-510 [hereinafter Joint Venture Registration Regulations].

This law is also known as the Procedures of the People's Republic of China for the Registration and Administration of Joint Ventures Using Chinese and Foreign Investment. FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 13, 17; Measures of the People's Republic of China on the Administration of the Registration of Sino-Foreign Joint Equity Ventures, 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-510.

52. *Zhonghua Renmin Gonghe Guo Zhongwai Hezi Jingying Qiye Fa Shishi Tiaoli* [Regulations for the Implementation of the Law of Joint Ventures Using Chinese and Foreign Investment], *promulgated* by the State Council on Sept. 20, 1983, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-550 [hereinafter Joint Venture Law Implementation Regulations].

53. *Zhonghua Renmin Gonghe Guo Zhongwai Hezi Jingying Qiye Laodong Guanli Guiding* [Regulations of the People's Republic of China for Labor Management in Joint Ventures Using Chinese and Foreign Investment], *promulgated* by the State Council on July 26, 1980, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-520 [hereinafter Joint Venture Labor Management Provisions]; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 20, 24.

This law is also known as Sino-Foreign Joint Equity Venture Labour Management Regulations, and Regulations of the People's Republic of China on Labour Management in Sino-Foreign Joint Equity Enterprises. See 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-520.

54. *Zhonghua Renmin Gonghe Guo Guowu Yuan Guanyu Guanli Waiguo Qiye Changzhu Daibiao jigou De Zanxing Guiding* [Interim Regulations of the People's Republic of China Concerning the Control of Resident Offices of Foreign Enterprises], *promulgated* by the State Council on Oct. 30, 1980, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 7-500 [hereinafter Resident Office Control Provisions], FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 166, 172.

These Provisions are also known as the Provisional Regulations of the State Council of the People's Republic of China for the Control of Resident Representative Offices of Foreign Enterprises, 1 CCH CHINA LAWS, *supra* note 18, at 521.

personnel).⁵⁵

3.3. *International Agreements*

While most Chinese legislation governing or relating to foreign investment conforms to international rules and practice, one should not forget an independent and important source of legal provisions regulating foreign investment in the P.R.C. — the various bilateral and multi-lateral international agreements and treaties concluded between Chinese and foreign governments. It is observed that "China is increasingly entering into international conventions" in the fields of foreign trade, taxation, investment protection, and the like.⁵⁶ It currently maintains foreign trade relations with 186 countries and regions in the world, and the existing trade agreements in force could possibly affect investment in the P.R.C.⁵⁷ In addition, it has concluded bilateral investment protection agreements with many countries in the past few years, and numerous other agreements are presently being negotiated or proposed.⁵⁸

In the area of taxation, the P.R.C. has entered into, and is still in the process of negotiating, a number of bilateral agreements for the avoidance of double taxation.⁵⁹ It has also ratified or acceded to multi-lateral international private law conventions such as the Paris Convention for the Protection of Industrial Property Rights of 1883⁶⁰ and the

55. *Waihui Guanli Zanxing Tiaoli* [Provisional Regulations for Foreign Exchange Control of the People's Republic of China], *adopted* at the Regular Session of the State Council on December 5, 1980, *promulgated* by the State Council on December 18, 1980 [hereinafter *Foreign Exchange Control Regulations*], and *reprinted and translated* in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-550; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 118, 130.

56. Horsley, *Comments on Laws and Developments*, *supra* note 19 at 179.

57. The United States has been one of the P.R.C.'s largest trade partners since the establishment of diplomatic relations between the two countries and the conclusion of the United States-People's Republic of China Agreement on Trade Relations on July 7, 1979, 31 U.S.T. 4651, T.I.A.S. No. 9630.

58. As of October 1987, nineteen investment protection agreements had been concluded between the P.R.C. and various foreign countries. These countries include the Benelux Economic Union, Canada, the Federal Republic of Germany, Finland, France, Italy, Romania, Sweden and the United Kingdom. *See* People's Daily, Oct. 18, 1987, at 4. An investment protection agreement was recently concluded between the P.R.C. and Japan. *See Sino-Japanese Investment Protection Agreement Signed in Beijing*, People's Daily, Aug. 29, 1988, at 1.

59. *See, e.g.*, Agreement for the Avoidance of Double Taxation, Apr. 30, 1984, United States-People's Republic of China, U.S.T. , T.I.A.S. No. , 23 I.L.M. 677 (1984). Other countries having similar agreements with the P.R.C. include Belgium (Apr. 18, 1985); Canada (May 12, 1986); Denmark (Mar. 26, 1986); Federal Republic of Germany (June 10, 1985); Finland (May 12, 1986); France; Italy (Oct. 31, 1986); Japan; Malaysia (Nov. 23, 1985); New Zealand (Sept. 16, 1986); Norway (Feb. 25, 1986); Thailand (Oct. 27, 1986); and the United Kingdom.

60. Paris Convention for the Protection of Industrial Property, Mar. 20, 1883, *as revised* at Stockholm on July 14, 1967, 21 U.S.T. 1630, T.I.A.S. No. 6923 [hereinafter *Paris Convention*], <https://scholarship.law.upenn.edu/jil/vol10/iss3/4>

United Nations Convention on Contracts for the International Sale of Goods of 1980.⁶¹

These agreements and conventions constitute an integral part of Chinese law governing foreign economic relations and should be taken into consideration by foreign investors and lawyers when doing business in the P.R.C.⁶²

3.4. Provincial and Municipal Legislation

Local legislation on foreign-related matters often directly regulate the formation and operation of foreign investment projects, and should not be overlooked.⁶³ Special attention should also be directed to legislation enacted by provinces, municipalities and autonomous regions as Guangxi, Guangdong, Fujian, Zhejiang, Shanghai, Jiangsu, Shandong, Hebei, Tianjin and Liaoning, where the special economic zones and coastal cities are located. Guangdong Province, due to its unique location and its important role in the nation's foreign trade and economic relations, has taken the lead in enacting local legislation and regulations on foreign investment.⁶⁴

It should be mentioned that Hainan, the P.R.C.'s second largest island formerly known as the Hainan Special Administrative Region under a dual jurisdiction of the central Government in Beijing and the Provincial Government in Guangdong has become a new province of

after Paris Convention].

61. United Nations Convention on Contracts for the International Sale of Goods, *reprinted in* 52 Fed. Reg. 6,264 (1987); U.N. CONVENTION ON CONTRACTS FOR THE INTERNATIONAL SALE OF GOODS, U.N. Doc. A/Conf.97/19, U.N. Sales No. E82.V5 (1980).

62. As of October 1987, China had ratified or acceded to 350 international conventions relating to foreign economic relations or business transactions. *See* People's Daily, Oct. 18, 1987, at 4.

63. The Constitution of the P.R.C. empowers the people's congresses of the provinces and municipalities directly under the Central Government, along with their standing committees, to "adopt local regulations, which must not contravene the constitution, the statutes and the administrative rules and regulations," Constitution of the P.R.C., *supra* note 18, art. 100. *See id.*, art. 116 (autonomous regions).

64. *See, e.g., Guangdong Sheng Jingji Te Qu Qiye Dengji Guanli Zanzing Guiding*, [The Provisional Regulations on the Registration of Enterprises in the Special Economic Zones of Guangdong Province], *adopted at* the Thirteenth Session of the Standing Committee of the Fifth Guangdong Provincial People's Congress on Nov. 17, 1981, *reprinted and translated in* 5 CCH CHINA LAWS, *supra* note 18, at ¶ 70-820 [hereinafter Guangdong SEZ Enterprise Registration Regulations]; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 215, 220. *See also Tianjin Jingji Jishu Kaifa Qu Guanli Tiaoli* [Regulations for the Administration of the Tianjin Economic and Technological Development Zone], *adopted by* the Twenty-First Session of the Standing Committee of the Tenth People's Congress of Tianjin on July 20, 1985, *reprinted and translated in* 5 CCH CHINA LAWS, *supra* note 18, at ¶ 92-003 [hereinafter

the People's Republic of China. The First Session of the Seventh National People's Congress recently announced the establishment of Hainan Province in April 1988.⁶⁵ It was decided that the proposed Hainan Province will become the largest SEZ in the P.R.C. and will be attributed a more special status than the existing SEZs.⁶⁶ It is anticipated that national and local legislation will be enacted concerning the status and development of the new province. Already, foreign businessmen and legal experts have expressed great interest in investing in the "virgin" island.⁶⁷

4. THE REGULATIVE STRUCTURE AND FOREIGN TRADE TRANSACTIONS CHAIN

The Chinese apparatus for foreign trade and foreign-related economic activities can be separated into five categories: 1) organs having general jurisdiction; 2) ministries and other ministry-level organs; 3) provincial and local State organs; 4) non-administrative national and local intermediaries; and 5) direct-and-end partners.

4.1. *The Supra-Ministerial State Organs*

At the State level and superior to all other organs is the State Council, which is responsible for directing and overseeing the administration of foreign trade and economic activities related to foreign trade.⁶⁸ One of its primary duties involves approving large scale foreign investment projects. All large scale foreign investment projects to be undertaken by ministries, provinces and special municipalities, or by FTOs and other economic entities which are subordinate to ministries and provincial administrations, are to be submitted to the relevant state and provincial planning bodies for examination.⁶⁹ Upon approval these projects are sent to the State Council for ratification.⁷⁰

65. See *China's Hainan Island Has Been Designated Province and Is To Become Country's Largest Special Economic Zone*, N.Y. Times, Apr. 22, 1988, at I4, col. 3.

66. *Hainan Will Become the Largest Special Economic Zone in Our Country*, People's Daily, Sept. 24, 1987, at 1 [hereinafter *The Largest Special SEZ*]. See also Statements Made by State Counselor Gu Mu, People's Daily, Oct. 30, 1987, at 1.

67. The Largest Special SEZ, *supra* note 66.

68. In the long run, all economic activities in the P.R.C. are subject to the State's central planning. Therefore, the approval of foreign investment projects is more or less within the central planning scheme. The State Council is constitutionally entrusted with the power to formulate and implement the State's economic plan in order to ensure "the proportionate and co-ordinated growth of the national economy." Constitution of the P.R.C., *supra* note 18, arts. 15, 89.

69. See *infra* notes 181-183 and accompanying text.

70. Moser, *Foreign Investment in China*, in FOREIGN TRADE, INVESTMENT, <https://scholarship.law.upenn.edu/jil/vol10/iss3/4>

Directly below the State Council are two powerful State commissions: the State Planning Commission (SPC) and the State Economic Commission (SEC). The SPC is responsible for formulating national economic plans and determining the nation's economic policy. The SEC is responsible for determining how to best implement the national economic plans established by the SPC. They also issue regulations and "measures" which are directly relevant to foreign investors.⁷¹ These two Commissions do not directly deal with foreign partners, nor do they directly administer the work of foreign trade and foreign economic co-operations. However, they play very important roles in the P.R.C.'s foreign trade and foreign economic relations during the planning stages.⁷²

4.2. Ministry-Level State Organs

Foreign economic transactions are regulated by the various foreign trade authorities operating under the central guidance of the Ministry of Foreign Economic Relations and Trade (MOFERT). The MOFERT was established in March 1982 as a result of the nation's reorganization scheme which merged two ministries and two state commissions into a single ministry.⁷³ Its major responsibilities include: 1) helping the SPC formulate national foreign trade and other foreign economic transaction plans; 2) formulating foreign investment laws and regulations, and supervising their implementation; 3) negotiating international trade agreements; 4) securing and approving foreign investment projects; 5) directing the foreign trade system; 6) approving im-

AND THE LAW IN THE P.R.C. 90, at 91 (1987).

71. See, e.g., *Guanyu Zhongwai Hezi, Hezuo Jingying Qiye Chanpin yi Chan ding Jin Banfa* [Measures on Replacement of Imports with Products of Sino-Foreign Joint Equity Venture Enterprises and Cooperative Enterprises], approved by the State Council, issued by the State Planning Commission on Oct. 19, 1987, *People's Daily*, Oct. 31, 1987, at 3; *Guanyu Zhongwai Hezi, Hezuo Jingying Qiye Ji Dian Chanpin yi Chan ding Jin Guanli Banfa* [Measures on the Administration of Replacement of Imports with Mechanical and Electrical Products of Sino-Foreign Joint Equity Venture Enterprises and Cooperative Enterprises], approved by the State Council, issued by the State Economic Commission in Oct. 1987. *Id.*

72. See Archer, *The Role of Administrative Agencies in Regulating Joint Ventures in China*, 21 STAN. J. INT'L L. 195, 196 (1985); Ellis, *Decentralization of China's Foreign Trade Structures*, 1981 J. INT'L & COMP. L. 288, 290.

73. The former ministries and commissions are the Ministry of Foreign Trade (MFT), the Ministry of Economic Relations with Foreign Countries (MERFC) and the State Foreign Investment Control Commission and the State Import-Export Commission. GUIDE TO CHINA'S FOREIGN ECONOMIC RELATIONS AND TRADE: IMPORT-EXPORT SPECIAL 331 (Policy Research Department, Ministry of Foreign Economic Relations and Trade ed. 1984) [hereinafter CHINA IMPORT-EXPORT GUIDE]. See also Ludlow, *China's New Foreign Trade Structure*, CHINA BUS. REV., May-June 1982,

port and export licenses; 7) participating in international trade organizations; 8) handling technology transfers; 9) coordinating with the Customs Administration and Commodity Inspection Agency; and 10) supervising, controlling and coordinating with specialized national foreign trade corporations (FTCs) and other related companies.⁷⁴

There are also other important ministry-level organs which a foreign investor should be familiar with. The State Administration of Industry and Commerce (SAIC) functions as the general registrar of all enterprises in the P.R.C., whether Chinese, Chinese-foreign, or wholly foreign.⁷⁵ The State Administration of Exchange Control (SAEC) exercises its powers on matters of foreign exchange, a dilemma foreign investors will no doubt encounter.⁷⁶ The Bank of China (BOC), a State-owned specialized foreign exchange bank of the P.R.C., serves as both a State organ and an enterprise. Its central tasks are "to raise, utilize, accumulate and manage foreign exchange funds, to engage in all kinds of foreign exchange business, and to participate in international financial activities for the purpose of rendering service to the modernization of China's socialist construction."⁷⁷ The State Administration of Commodity Prices (SACP) handles the overall administration of pricing matters when the foreign-invested enterprise's products are marketed within the P.R.C.⁷⁸ The Ministry of Finance (MOF) and the General Taxation Bureau (GTB) thereunder formulate the State's tax policy and promulgate rules and regulations for implementing tax legislation by the N.P.C.⁷⁹

4.3. Provincial and Local Organs

Each province, autonomous region and municipality directly con-

74. See China Import-Export Guide, *supra* note 73.

75. See 1984 ALMANAC, *supra* note 35 at 217, 655.

76. *Id.* at 656.

77. Articles of Association of the Bank of China, *approved by* the State Council on Sept. 22, 1980, art. 2, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-500; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 99, 104. The Scope of the Bank of China's business includes: 1) international settlements of foreign trade and non-trade-related transactions, 2) deposits and loans among international banks, 3) international remittances, 4) deposits and loans in foreign currencies RMB and foreign exchange-related deposits and loans, 5) buying and selling of foreign exchanges, 6) buying and selling of gold on international markets, 7) organizing or participating in international syndicated loans, 8) investing solely or jointly in banks, finance companies, other enterprises in foreign countries and in regions such as Macao and Hong Kong, 9) issuing bonds and securities in foreign currencies, and 10) providing trust and consulting services. *Id.*, art. 5.

78. See 1984 ALMANAC, *supra* note 35, at 217, 655.

79. The GTB's status was recently upgraded to a ministry-level bureau which now directly reports to the State Council than the Finance Ministry.

trolled by the State Council maintains either a Foreign Economic and Trade Commission (COFERT) or a Foreign Economic and Trade Department (DOFERT),⁸⁰ and each local city or county maintains a Foreign Trade Bureau (local FTB). These provincial COFERTs, DOFERTs and local FTBs play a direct role in the creation, modification, and maintenance of locally foreign-invested projects.⁸¹

Provincial and local Administrations for Industry and Commerce (local AICs) are authorized by the SAIC to register foreign-invested enterprises in their localities and to issue licenses. They also partake in the operation of such foreign-invested entities in terms of regulatory administration.⁸² Provincial and local Tax Bureaus possess direct supervisory, inspection and penal powers in all tax matters relating to the operation of foreign-invested enterprises.⁸³ Lastly, the Departments of Labor and Personnel at both the provincial and local levels exercise specific jurisdiction over the foreign-invested enterprises' operation in matters of labor management concerning domestic Chinese employees. They approve labor plans, labor contracts and the implementation of such plans. In addition, these departments supervise and inspect the implementation of rules and regulations concerning labor protection.⁸⁴

80. While the foreign trade authorities in a majority of provinces and autonomous regions are called "Foreign Economic and Trade Departments," Beijing, Shanghai, Tianjin and a number of provinces each have a "Commission." Some also have an alternative foreign trade organ either under or in conjunction with the main commission or department. For example, the Liaoning Provincial Foreign Trade Bureau operates under the Liaoning Provincial COFERT, the Shandong Provincial Foreign Economic Office operates in conjunction with the Shandong Provincial DOFERT, the Tianjin Foreign Trade Bureau operates under the Tianjin COFERT and the Guangdong Provincial Foreign Economic Commission operates in conjunction with the Guangdong Provincial Foreign Trade Bureau. See 1984 ALMANAC, *supra* note 35, at 219-21, 658-60.

81. See *infra* text accompanying notes 181-83; See also Archer, *supra* note 72, at 200-03, 205-06. The difference between the commission, department and bureau is primarily a matter of choice in terminology. A provincial government is generally composed of various functional departments. When the designation "commission" is attached, it is usually indicative of greater authority, more responsibilities and sometimes signifies a larger institution. For the sake of simplicity, these COFERTs, DOFERTs and FTBs are collectively referred to as "foreign trade bureaus" (FTBs) and their functions are more or less similar in nature.

82. See Joint Venture Registration Regulations, *supra* note 51, arts. 2, 7, 9, 10. See also *infra* notes 202-11 and accompanying text.

83. See Joint Venture Income Tax Law, *supra* note 45, arts. 1, 11, 12, 14; *Zhongguai Hezi Jingying Qiye Suode Shui Fa Shixing Xize* [Detailed Rules and Regulations for the Implementation of the Income Tax Law of the People's Republic of China Concerning Joint Ventures with Chinese and Foreign Investment], approved by the State Council on Dec. 10, 1980, promulgated by the Ministry of Finance on Dec. 14, 1980, arts. 31, 34, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 33-510 [hereinafter Joint Venture Income Tax Rules]; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 45, 55.

84. See Legal Joint Venture Registration, Management Provisions, *supra* note 53, art.

5. CHINESE PARTNERS AND INTERMEDIARIES

5.1. Foreign Trading Organizations

Since the 1950s, the P.R.C.'s foreign trade and foreign-related economic activities have been conducted through an apparatus known as foreign trade corporations (FTCs), which are similar to the foreign trade organizations (FTOs) in the Soviet Union and the East European countries. These were primarily created under the predecessors of the MOFERT at the national level, with branches in the provinces and local counties and cities. The FTCs were once the primary, if not the sole, organizations responsible for dealing with foreign firms. They were and still are authorized to execute contracts with foreign partners.⁸⁵

Today, certain changes should be observed. The FTC label is no longer an accurate description for many import-export corporations, though they are still identified as such by foreign businessmen for the sake of convenience. The business scope of these corporations has been expanded. Some of the "specialized" FTCs conduct business that is unrelated to their purported specialties. For example, the China National Aero Technology Import & Export Corporation (AEROT) conducts import and export business of aeroproducts and technology as well as non-aeroproducts and technology.⁸⁶ Also, the FTCs do not merely conduct business involving conventional foreign trade. Some do not even engage in the traditional import and export of goods. Their business has been expanded to include, for example, technology transfers and domestic and foreign investment. Second, the FTC is no longer the only means through which Chinese enterprises may conduct business with foreign firms. A limited yet increasing number of Chinese producers, such as the Qingdao (Tsingtao) Beer Factory, are empowered to directly contact foreign importers for trade or other transactional negotiations.⁸⁷ Third, the number of FTCs has been significantly increased.⁸⁸ Newly created FTCs have periodically been recognized by the Chinese

13.

85. See generally, Horsley, *The Regulation of China's Foreign Trade*, in FOREIGN TRADE, INVESTMENT AND THE LAW IN THE P.R.C., *supra* note 70 at 9-11 [hereinafter Horsley, *China's Foreign Trade*]; Tay, *Introducing China's Business Laws and Practice*, in 1 CCH CHINA LAWS, *supra* note 18, at ¶¶ 2-420, 2-425, 2-435.

86. 1984 ALMANAC, *supra* note 35, at 693.

87. See People's Daily, Oct. 5, 1987, at 3.

88. For an incomplete and to-be-updated list of FTCs, see 1984 ALMANAC, *supra* note 35 at 235-80 (in Chinese), 685-717 (in English). Information is also available from THE CHINA PHONEBOOK AND ADDRESS DIRECTORY (1986), THE CHINA INVESTMENT GUIDE (1986), and U.N. GUIDEBOOK ON TRADING WITH THE PEOPLE'S REPUBLIC OF CHINA (1984).

press.⁸⁹ Fourth, the MOFERT and virtually all the other ministries, particularly the industry ministries, maintain their own subordinate enterprises which are capable of promoting economic cooperation with foreign partners. These specialized enterprises, which include import-export corporations, are under the central ministerial control of their respective ministries and primarily handle foreign trade and investment activities.⁹⁰

The largest and most significant FTC is the China International Trust and Investment Corporation (CITIC). The 1979 creation of CITIC has had the same importance as the promulgation of the Joint Venture Law.⁹¹ The CITIC is a State-owned enterprise under the leadership of the State Council whose purpose is "to guide, absorb and utilize foreign funds, bring in advanced technology and import advanced equipment" for the purpose of advancing foreign investment in the P.R.C.'s development.⁹² Although it is not an administrative organ, the fact that it is directly accountable to the State Council and that it has close working relations with the SPC, the MOFERT, the SEC, the People's Bank of China (PBC), and the BOC, as well as with central and local enterprises, indicates that CITIC occupies strategic positions which will enable it to foster cooperation with foreign investors. To quote the Chairman of the Board of CITIC, being "[q]uite well informed, it can be both a partner in economic cooperation and an advisor or counselor for foreign entrepreneurs."⁹³

Other important FTCs include the China National Technology Import and Export Corporation (TECHIMPEX),⁹⁴ the China National Machinery Import and Export Corporation (MACHIMPEX), the China National Instrument Import and Export Corporation (INSTRIMPEX), the China National Textiles Import and Export Corpo-

89. See, e.g., *People's Daily*, Oct. 17, 1987, at 1.

90. U.S. DEPARTMENT OF COMMERCE INDUSTRIAL TRADE ADMINISTRATION, *DOING BUSINESS WITH CHINA* 4 (1980).

91. See Tay, *supra* note 85, at ¶ 2-420.

92. Articles of Association of the China International Trust and Investment Corporation, arts. 1, 2., *FOREIGN ECONOMIC LEGISLATION*, *supra* note 36, at 108, 114.

93. Rong, *China's Open Policy and CITIC's Role*, 1986 J. INT'L AFF. 57, 58, 61 (1986). It may be noted that, while most FTCs have branches in each province, the local investment and trust corporations are not affiliated with CITIC; they are administered by provincial or local governments. There is, however, cooperation between the CITIC and local corporations. *Id.* at 61.

94. Its predecessor was the China National Technical Import Corporation (TECHIMPORT). Due to the increasing, but still minor, need abroad for Chinese technology, the State officially expanded the Corporation's business scope by adopting its current name, TECHIMPEX. See *TECHIMPORT Actively Seeking Export of Technology*, *People's Daily*, Sept. 5, 1987, at 1. Even before TECHIMPORT changed its name, it had been handling the export of Chinese scientific and technical patents.

See 1984 ALMANAC, *supra* note 35, at 237, 687.

ration (CHINATEX), the China National Light Industrial Products Import and Export Corporation (INDUSTRY), the China National Chemical Import and Export Corporation (SINOCHEM) and the China Electronics Import and Export Corporation (CEIEC).⁹⁵

5.2. *The China Council for the Promotion of International Trade*

The China Council for the Promotion of International Trade (CCPIT) was created in 1952. Although it is generally considered to be semi-official, it is a non-governmental economic and trade organization composed of representatives and experts from the P.R.C.'s economic and trade circles.⁹⁶ It functions similarly to the Chambers of Commerce in other countries.⁹⁷ The CCPIT attempts to promote Chinese economic and trade relations with foreign countries under the "principle of equality and mutual benefits" and to enhance mutual understanding and friendship between the Chinese and other peoples.⁹⁸ It organizes local trade fairs and exhibitions such as the annual Guangzhou Trade Fair, which provide opportunities for both Chinese and foreign parties to identify areas for potential investment. It also conducts technical seminars and international meetings, provides legal advice, resolves commercial disputes,⁹⁹ and connects Chinese end-users or producers with foreign partners.¹⁰⁰

5.3. *End-Users, Manufacturers and Local Partners*

It is a real possibility that the P.R.C.'s local manufacturers and end-users could become direct partners in Sino-foreign equity or contractual joint venture enterprises. The Joint Venture Law provides that a joint venture may be established between "foreign companies, enter-

95. 1984 ALMANAC, *supra* note 35, at 685, 686, 693.

96. The CCPIT is a "people-oriented" autonomous organization sponsored and financed by the MOFERT and other trade and economic institutions. Its board of directors includes officials from the MOFERT, the Bank of China, and other relevant departments. See Horsley, *China's Foreign Trade*, *supra* note 85, at 13.

97. In fact, the CCPIT began using the name "China Chamber of International Commerce (CIC)" in late June 1988. Both names are currently in use, depending on the circumstances involved. See *CCPIT Provides Multiple Services*, People's Daily, Sept. 15, 1988, at 3.

98. 1984 ALMANAC, *supra* note 35, at 219.

99. Two subsidiary arbitration commissions, the Foreign Economic and Trade Arbitration Commission (FETAC) and the Maritime Arbitration Commission (MAC), under the CCPIT's direction handle all international commercial and maritime disputes which are brought before them. See *infra* text accompanying notes 457-72.

100. See 1984 ALMANAC, *supra* note 35, at 219, 657-58. See also Wang, *CCPIT's Tasks, Achievements and Outlook*, CHINA IMPORT-EXPORT GUIDE, *supra* note 73, at 43, 378; Archer, *supra* note 72, at 217.

prises and other economic entities or individuals" and "[C]hinese companies, enterprises and other *economic entities*."¹⁰¹ The "other economic entities" clause may be interpreted to include the Chinese factories and communes which serve as the basic industrial and agricultural economic organizations.

Traditionally, Chinese end-users, dealers and manufacturers in the chain of trade and local partners in Sino-foreign joint or co-operative projects have established their contacts with foreign businesses through various FTCs or other intermediaries.¹⁰² This is still a common practice today. The practice is not an unusual one in a non-market economy where planning and centralization are the major themes. Recent years, however, have witnessed a gradual move towards decentralization in the P.R.C.'s foreign trade and foreign economic relations. The number of foreign trading corporations has increased from fewer than 100 to more than 800 by the end of 1986.¹⁰³ In addition, many Chinese manufacturers, such as the Anshan Steel and Iron Corp., the largest of its kind in the P.R.C., and the Qingdao (Tsingtao) Beer Factory, have been granted full power to conduct their export businesses directly without FTC representation.¹⁰⁴ This result is due, in part, to the State's new policy of combining industry or agriculture with foreign trade.¹⁰⁵

Some FTCs and upper-level Chinese enterprises themselves enter into joint ventures with foreign investors as a direct partner rather than as an intermediary. Currently, one of the major impediments to complete decentralization is the highly centralized control of foreign exchange earned by export-oriented producers. The producing factory itself does not maintain foreign exchange reserves - FTCs and the State do. In order to resolve this problem, the MOFERT and the State have already initiated an "Exporting System Reform Trial Plan" ("Reform Plan") beginning in 1988, which is directed towards combining manufacturing enterprises with foreign trade.¹⁰⁶ It is hoped that this plan

101. Joint Venture Law, *supra* note 36, art. 1. See also Lussenburg, *Joint Venture Investment in the People's Republic of China: A Continuing Challenge*, 63 CAN. B. REV. 545, 551 (1983); Torbert & Thompson, *China's Joint Venture Law: A Preliminary Analysis*, 12 VAND. J. TRANSNAT'L L. 819, 841-42 (1979).

102. See Tay, *supra* note 85, at ¶ 12-435.

103. See People's Daily, Oct. 13, 1987, at 1.

104. See *supra* note 87 and accompanying text. See also *Anshan Plant Complaints of Government Red Tape*, Foreign Broadcasting Information Service, Dec. 5, 1980, at L-5 [hereinafter FBIS]; *Twenty-Six Machine Building Enterprises Transact Export Business*, China Econ. News, June 9, 1980, at 7-8.

105. See People's Daily, Oct. 13, 1987, at 1.

106. See *China's Exporting System Reform Will Take Place Next Year* (Woguo Chutou Tizhi Mingnian Gaige) People's Daily, Dec. 2, 1987, at 1.

will allow more export-oriented enterprises to become direct foreign trading partners and to maintain their own foreign exchange reserves to a certain degree (70% to 100%). According to the Reform Plan, the clothing, electronics, automotive, as well as most light industries will be among the first trades slated for export reform trials.¹⁰⁷

Another major obstacle to decentralization is the fact that, unlike the FTCs and other upper level enterprises, most local factories and communes as well as other economic entities lack the experience, specialized personnel, and skills necessary to deal effectively with foreign traders and entrepreneurs. Improvement in this situation will take time.

6. FORMS OF FOREIGN INVESTMENTS

There are three principal investment vehicles known as the "*San Zi Qiye*" ("three-forms of foreign investment enterprises"), which are available to foreign investors in the P.R.C.: the equity joint venture, the contractual or non-equity joint venture, and the wholly foreign-owned enterprise. The equity joint venture is considered by the Chinese to be the most significant and most favored vehicle for absorbing foreign investment. A large and comprehensive set of regulatory rules has been promulgated for the creation and operation of Sino-foreign equity joint ventures, including the Joint Venture Law Implementation Regulations, the Joint Venture Registration Regulations and the Joint Venture Labor Management Provisions.¹⁰⁸ The contractual joint venture, though still lacking detailed legal standards, is nevertheless the most widely-used vehicle for foreign investment. Specific legislation such as the Wholly Foreign-Owned Enterprise Law,¹⁰⁹ has been adopted regulating the wholly foreign-owned subsidiaries which are rapidly becoming popular in certain areas.

In addition to these three principal investment vehicles, there also exist some alternative investment vehicles which are often favored by smaller partners such as processing against provided samples (*lai yang jiaogong*), processing with provided materials (*lai liao jiaogong*), assembling with provided parts or components (*lai jian zhuangpei*) and compensation trade (*bu chang maoyi*). These arrangements are also known as "*San Lai Yi Bu*" (three "lai's" and one "bu"). For the purposes of this article, these processing and assembling and compensation trade transactions will be treated within the framework of the contractual joint venture, although in the P.R.C. they are not regarded as "joint

107. *Id.*

108. See *supra* notes 37, 38, 39.

109. See *supra* note 39.

venture" vehicles on the same level with the Sino-foreign joint ventures and Sino-foreign co-operative enterprises.

6.1. *Equity Joint Ventures*

So much has been written on Chinese equity joint ventures that the author feels somewhat excused from giving a detailed explanation of this subject.¹¹⁰ The importance of these ventures, though, does not allow for its wanton omission in a consideration of the P.R.C.'s foreign investment framework. It is in this area that the P.R.C. has enacted the most complete set of laws and regulations. Of these laws, the Joint Venture Law of 1979 is the most important, setting forth the general principles concerning the establishment and operation of joint venture enterprises.¹¹¹ It provides guidelines for approval procedures, capital structure, management, profit distributions, labor relations and dispute settlement.¹¹² Equally relevant is the 1983 Joint Venture Law Implementation Regulations. As amended in 1986, they expand the 15 articles of the Joint Venture Law and correct errors in the earlier legislation.¹¹³

Equity joint ventures normally require substantially more capital investment than do other forms of investment. The advantage of the equity joint venture arrangement, in addition to pooled assets, shared profits and losses and joint management, is the establishment of a new limited liability company¹¹⁴ for an agreed upon duration set out in the contract.¹¹⁵ Equity joint ventures by nature contemplate that a common board of directors, managers and laborers directly employed by the new entity, joint use of financial resources, sharing of profits and losses, and limited liability equal to the amount of capital contribution will be

110. See generally, Alford & Birenbaum, *supra* note 39; Klingenberg & Pattison, *Joint Ventures in the People's Republic of China: The New Legal Environment*, 19 VA. J. INT'L L., 807, 814 (1979); Lussenburg, *supra* note 101; Rich, *supra* note 22; Shen, *China's New Law on Joint Ventures Using Chinese and Foreign Investment*, 34 SW. L.J. 1183 (1981); Torbert & Thompson, *supra* note 101; Wilson, *supra* note 30.

111. Joint Venture Law, *supra* note 36.

112. The Joint Venture Law is beyond the regulation of joint ventures. See *supra* notes 36-39 and accompanying text. As one commentator has remarked, "[it] was not merely fifteen articles regulating a particular form of business enterprise; rather, it symbolized the new Chinese open-door policy of economic cooperation with foreign investors." Goossen, *Canadian Business Negotiations in Post-Mao China: A Progress Report on the New Foreign Economic Legislation*, 31 MCGILL L.J. 1, 8 (1985).

113. Joint Venture Law Implementation Regulations, *supra* note 52.

114. An equity joint venture has to be a newly created limited company with the status of a Chinese legal person. Joint Venture Law, *supra* note 36, art. 4; Joint Venture Law Implementation Regulations, *supra* note 52, art. 2.

115. Joint Venture Law, *supra* note 36, art. 12.

among their key characteristics.¹¹⁶

Both parties must exercise caution in negotiating the complex and sophisticated provisions of an equity joint venture agreement. For example, the share ratio of the new limited company and the method of contributing capital must be determined. Capital contributed by the parties can be in cash, in kind, in industrial properties such as factory buildings, machines and equipment; or in the right to use land, patented technology and trade secrets or know-how. Also, the duration of the contractual relationship may be long or short, depending on the parties' plans.¹¹⁷ In such an arrangement, the Chinese partner usually provides the site, factory buildings, raw materials, cash and/or know-how as its investment, and its foreign counterpart provides the technology, equipment, industrial property, and/or capital in foreign currencies.

The Chinese government considers the equity joint venture "a means by which Chinese companies could absorb advanced technology and Western managerial skills and become major foreign exchange earners in the world's leading markets."¹¹⁸ This form of investment is not only favored by the Chinese, but is also attractive to foreign investors. For the latter, it is a means of ensuring a degree of political protection through the linkage with local interests, access to resources that would otherwise be unavailable or very difficult to obtain in the open market, access to the inexpensive local labor force and a guarantee of supply.¹¹⁹ In addition, the Chinese domestic market is open to equity joint ventures to a certain extent, and is quite close to other Southeast Asian markets as well. These factors make "joint venture investment more appealing than other forms of investment."¹²⁰

6.2. Contractual Joint Ventures

Contractual joint venture enterprises are non-equity joint ventures. They are often referred to in the Chinese context as cooperative enterprises (*hezuo qiye*), cooperative operation enterprises (*hezuo jingying qiye*), co-operative operations (*hezuo jingying*), co-operative development (*hezuo kaifa*) or sometimes simply co-productions (*hezuo shengchan*). The Chinese usually differentiate between Chinese-foreign

116. *Id.*, arts. 4, 6.

117. See FUNG, CHINA TRADE HANDBOOK 172 (Hong Kong ed. 1984).

118. Moser, *supra* note 70, at 100.

119. See Klingenberg & Pattison, *supra* note 110, at 814.

120. Lussenburg, *supra* note 101 at 551. For problems such as joint venture management, capital contributions, minimum and maximum of capital and the nationality of the president of a joint venture, see *infra* notes 212-57 and accompanying text.

co-operative enterprises, which are the dominant form of foreign investment, and joint or co-operative development projects, which are mainly concerned with the exploration and development of off-shore oil. This differentiation will be recognized in this article.

6.2.1. *Co-Operative Enterprises*

Most non-equity joint ventures are distinguished by three characteristics: 1) pooled assets; 2) shared profits and losses; and 3) joint management. Non-equity joint ventures also share similarities with equity joint ventures. A common characteristic is joint management and investment in cash, tangible property and intangible property by both forms. Despite the similarities, the two forms are treated in a fundamentally different manner under Chinese law and practice. The primary distinction between an equity and a non-equity joint venture is that the latter does not necessarily allocate shares by the amount invested, or divide profits in accordance with the number of shares owned, but either divides profits according to the form of investment and the percentage of distribution as provided for in the contract, or shares profits according to the amount of products and income produced.¹²¹

A contractual joint venture need not be incorporated as a limited company. The only thing that is necessary is a simple agreement or contract that sets out the rights and obligations of the contracting parties. Usually, the contract will combine the funds, equipment and technology of the foreign partner with the labor, physical facilities and raw materials of the Chinese partner.¹²²

In order to promote equality and mutual benefit, co-operative enterprises are jointly run by both Chinese and foreign firms. The responsibilities, rights and obligations, including the division of profits, of both parties are stipulated in the contract. Currently, all properties belonging to such enterprises are turned over to the Chinese partner upon the expiration of the period of co-operation.¹²³

As for the legal status of a contractual joint venture, the focus is not on whether it is considered a legal person. Since the Chinese partners are essentially Chinese enterprises which enjoy the status of legal persons, it is often difficult to discern whether a particular Sino-foreign co-operative enterprise is considered a Chinese legal person. Thus, it is easier and more important to determine whether the joint venture cre-

121. Research Office Under Guangdong Provincial Foreign Economic Relations Commission, *Co-Production: A Good Form for Absorbing Foreign Investment* 1984 ALMANAC, *supra* note 75, at 211, 649 [hereinafter Guangdong Research Office].

122. FUNG, *supra* note 117 at 172.

123. Guangdong Secretariat Office, *supra* note 121, at 212, 650.

ates a "new" and separate legal person. The Co-Operative Enterprise Law contains an article which provides that "[a Sino-foreign] co-operative enterprise which complies with the conditions for becoming a legal person under the relevant provisions of Chinese law shall obtain the status of a legal person in accordance with the law."¹²⁴ This implies that a contractual joint venture may also choose to become a partnership-type enterprise which, under the General Principles of Civil Law, does not enjoy the status of a Chinese legal person.¹²⁵

There are two forms of contractual joint venture enterprises: 1) joint entities having the status of a new legal person, which are "very much like an equity joint venture company" and 2) associations whose form does not result in the creation of a new legal person.¹²⁶ In the first form, the contracting parties will usually limit their liability to the amount of their capital contributions through a contractual provision, and the contributions of both sides are owned by the newly created independent legal entity. The parties may also limit their liability vis-à-vis third parties. A provision of the Co-Operative Enterprise Law permits the parties involved to agree upon the terms of entrusting to third parties the responsibility of managing the enterprise.¹²⁷

In the second form, the business relationship between the two parties embraces the form of an association which conforms to the terms established by the contract, with each party registering with the appropriate Chinese authorities and with the joint venture's operations being carried out in accordance with the contractual provisions.¹²⁸ Since no legal person is created in this case, the co-operative enterprise or association does not own equity or registered capital. Instead, the property is owned by each partner, and the contributions of both parties are in kind (equipment, raw materials, labor, etc.) rather than in cash. The enterprise or association only has the authority to administer and use the property.¹²⁹

124. Co-Operative Enterprise Law, *supra* note 38, art. 2(2).

125. For example, a contractual joint venture may lack civil standing for certain rights and obligations, and would therefore be disqualified from benefiting from the independent legal person status. See General Principles of Civil Law, *supra* note 43, art. 37.

126. The second type is the "purely contractual" joint venture, commonly known to the Chinese as a co-operative production enterprise, where no novel legal entity is created. In Poland, this is known as a "partnership" (an imperfect juridical person).

127. Co-Operative Enterprise Law, *supra* note 38, art. 12(2).

128. See Moser, *supra* note 70, at 97 (Forms of Co-Operative joint ventures).

129. See Nee, *The Forms of Foreign Investment in China: Practice Commentary*, COMMERCIAL BUSINESS AND TRADE LAWS: PEOPLE'S REPUBLIC OF CHINA 26 (1987); Yue, *The ABC of Investing in China (III): Three Forms of Investment Called For*, BEIJING REV., June 1, 1987, at 21, 22 [hereinafter Yue, *The ABC of Investing in China (III)*].

A co-operative enterprise may, however, enjoy the status of a legal person if, after consultation, both sides choose to do so. In this scenario, each side will bear its responsibilities independently.¹³⁰ In the past, some co-operative enterprises have chosen to take the form of a limited liability company, which includes a board of directors, thus making it possible for it to pay income tax under the Joint Venture Income Tax Law¹³¹ rather than the Foreign Enterprise Income Tax Law.¹³² The only difference is that the parties to such co-operative productions are not afforded an equity interest in the enterprise based on the monetary value of their respective investment contributions since they are not required to distribute the profits strictly in accordance with their respective equity interests.¹³³ Regardless of the accuracy of the distinction discussed above, most contractual joint ventures in the P.R.C. have taken the second form.

Legislation and sub-legislation regulating contractual joint ventures has been the least developed of the laws governing foreign investment in the P.R.C. Prior to the adoption of the 1988 Co-Operative Enterprise Law, nothing existed in published form which provides an overview of how a contractual joint venture is regulated in terms of application, approval and operation. This was believed to be a result of the "complex and diverse nature" of contractual joint ventures.¹³⁴

Nevertheless, provisions regulating equity joint ventures have been applied by analogy. Internal documents (*neibu wenjian*) have also been circulated among Chinese negotiators and other relevant parties to unofficially provide basic and practical guidelines for the creation and operation of contractual joint venture enterprises on a temporary basis. Meanwhile, the Draft of the Law of the People's Republic of China on Sino-Foreign Co-Operative Enterprises,¹³⁵ prior to its adoption in

130. See Guangdong Research Office, *supra* note 121, at 211, 649.

131. Joint Venture Income Tax Law, *supra* note 45.

132. Foreign Enterprise Income Tax Law, *supra* note 46. Enterprises under the Joint Venture Income Tax Law enjoy greater tax benefits than those governed by the Foreign Enterprise Income Tax Law. See *infra* notes 309-39 and accompanying text.

133. The Joint Venture Law, *supra* note 36, art. 4, requires that the net profit of a joint venture be distributed to the parties in an amount proportionate their respective contributions to the registered capital, whereas the Co-Operative Enterprise Law, *supra* note 38, art. 2, which lacks such requirements, permits the parties to prescribe the terms for profit distribution and the sharing of profit losses in the co-operation contract.

134. Zheng, *Foreign Investment Law in the People's Republic of China: A 1986 Update*, 19 N.Y.U. J. INT'L L. & POL. 269, 273 (1987).

135. For a discussion of the drafting of the Law of the People's Republic of China on Sino-Foreign Co-Operative Enterprises (Zhong Wai Hezuo Jingying Qiye Fa Cao'an), see Wei, 1984 ALMANAC, *supra* note 35, at 18, 129; Nee, *supra* note 129, at 25. See also *China's Foreign Economic Laws and Regulations Becoming Sound*, *People's Daily*, Aug. 12, 1986, at 1, *Sino-Foreign Co-Operative Enterprise Law*

April 1988 had been prepared and discussed for several years.

In fact, the lack of official regulations provided a greater degree of flexibility for parties in contractual joint venture relationships. The parties may, subject to the Chinese government's approval, insert into a contract any provisions concerning the rights, responsibilities, and obligations of each party and maintain that they be free from the influence of subsequent Chinese legislation.¹³⁶ For example, unlike the case concerning an equity joint venture which involves a statutorily imposed minimum for foreign holdings (25%) along with other rights and responsibilities, the rights of parties to a co-operative enterprise are stipulated in the contract, and there is no minimum foreign holding required. According to Wei Yuming, formerly a Vice-Minister of MOFERT and now the President of the China Association of Foreign Investment Enterprises, "[p]roblems that should have been solved by the . . . [Co-Operative Enterprise Law] still in absence for the time being can be written into contracts. Once upon approval by the Government, the contracts have the same legal effect."¹³⁷ The promulgation of the Co-Operative Enterprise Law does not appear to have diminished the degree of flexibility. Under the new law, the management of a contractual joint venture is given full autonomy. It may choose to include a board of directors or simply a joint managerial system, and the chairman of the board or director of the joint management team may be either the Chinese or foreign party; third parties may also manage the venture.¹³⁸ This flexibility is one of the primary factors that maintains the dominance of the joint venture over other forms of foreign investment.¹³⁹

(Draft) submitted for consideration, People's Daily, Jan. 12, 1988, at 1; Zheng Tuobing, Minister of MOFERT, *Commenting on the Bill of the Co-Operative Enterprise Law (Draft)*, People's Daily, Apr. 1, 1988, at 1; Yuan Zhenmin, Director, Department of Law and Treaties, *MOFERT Commenting on the Co-Operative Enterprise Law (Draft)*, People's Daily, Apr. 2, 1988, at 8 [hereinafter Yuan Zhenmin Commenting].

136. The Foreign Economic Contract Law reads as follows:

When new relevant provisions are stipulated by law, the Sino-foreign equity or contractual joint venture contracts and the contracts of cooperative exploration and development of natural resources which are approved by the State and performed within the territory of the People's Republic of China may still be performed on the basis of the original contract.

Foreign Economic Contract Law, *supra* note 42, art. 40.

137. Wei, *supra* note 35, at 18, 399.

138. Co-Operative Enterprise Law, *supra* note 38, arts. 10, 12, 12(2).

139. The co-operative enterprise has been, and still remains, the most popular form of foreign investment in the P.R.C. By the end of 1985, there were 3,030 co-operative enterprises and 31 off-shore oil projects, which are similar to contractual joint ventures. The combined total of 3,061 is almost twice that of the 1,618 equity joint ventures entered into during the same period. See Rong, *supra* note 93, at 60. Another source shows that by the end of 1985, there were 3,700 Sino-foreign contractual joint

6.2.2. Co-operative Development (Off-Shore Oil Projects)

Co-operative development projects, which are primarily off-shore oil projects, are regulated by the 1982 Offshore Petroleum Regulations.¹⁴⁰ As with pure contractual joint venture arrangements, the co-operative development vehicle has been used solely in connection with cooperative offshore oil exploration, development, production, and marketing contracts. Unlike the contractual joint venture, where both sides provide capital contributions during the investment phase of the contract, both the Chinese party and the foreign oil company would provide capital contributions for the co-operative development of resources only if during the exploration stage, quantities of raw materials worthy of development are found. Once production has begun, the extracted oil is divided between the parties as stipulated in the contract.¹⁴¹ Under the Offshore Petroleum Regulations, the China National Offshore Oil Corporation (CNOOC), a State controlled enterprise possessing the exclusive right to develop and exploit the P.R.C.'s offshore petroleum within specified zones of co-operation with foreign enterprises,¹⁴² is authorized and is responsible for negotiating "petroleum contracts" with foreign oil companies. Unless otherwise provided in the contract or by the Ministry of the Petroleum Industry, the foreign contractor provides the capital investment needed to carry out exploration, to assume responsibility for exploration operations, and to bear all risks. The foreign contractor is also responsible for the development and production operations until CNOOC assumes the responsibility for such operations at a time specified in the contract.¹⁴³

The foreign contractor may recover its investment and expenses and receive remuneration from petroleum production. It may also export the petroleum it has extracted as well as the petroleum it purchases and may remit abroad its recovered investment and profits.¹⁴⁴

ventures, a figure slightly less than twice the number of Sino-foreign equity joint ventures and 30 times the number of wholly foreign-owned subsidiaries. *The Number of Foreign-Invested Enterprises Increasing Annually*, People's Daily, Aug. 6, 1986, at 3. According to Yuan Zhenmin, Law and Treaties Department Director, MOFERT, there were 5,193 contractual joint ventures as of January 1, 1988, a figure which was more than one-half the total number of foreign investment enterprises (10,008). See Yuan Zhenmin Commenting, *supra* note 135.

140. *Dui Wai Hezuo Kaicai Haiyang Shiyu Ziyuan Tiaoli* [Regulations of the People's Republic of China on the Exploitation of Offshore Petroleum Resources in Cooperation with Foreign Enterprises], adopted by the State Council on Jan. 12, 1982, promulgated on Jan. 30, 1982, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 14-560 [hereinafter 1982 Offshore Petroleum Regulations].

141. *Id.*, art. 7.

142. *Id.*, art. 5.

143. *Id.*, art. 7.

144. *Id.*, art. 8.

CNOOC has prepared a model contract as a guideline for negotiations with foreign oil companies in the co-operative development of the P.R.C.'s oil resources. The model contract provides that a fixed percentage of the recovered oil will initially be allocated to the Chinese partner for payment of the Consolidated Industrial and Commercial Tax¹⁴⁵ and as a royalty payment. Thereafter, a specified percentage of the oil is to be divided between the partners as compensation for the capital invested for exploration and development and charges for accrued interest. Finally, the remainder of the oil is divided between the parties according to a sliding profit formula that is determined during the bidding and negotiation process.¹⁴⁶ Although co-operative development projects probably afford the greatest flexibility of any of the currently available forms of foreign investment, its use has been limited to offshore oil projects.¹⁴⁷ This may change, however, as new laws may be developed regulating this vehicle of investment.

6.2.3. *Compensation Trade and Processing and Assembling Transactions*

Compensation trade and processing and assembling dealings are the simplest forms of foreign investment in the P.R.C., and last for shorter periods of time, not extending longer than five years. Of these forms, the compensation trade arrangement is the more popular one. It is "an intermediary step between traditional foreign trade and conventional capital investment."¹⁴⁸

The compensation trade arrangement first appeared as a vehicle for investment in the mid-seventies, limited to transactions between Hong Kong firms and enterprises in Guangdong and Fujian Provinces.¹⁴⁹

Since the late 1970s, the use of this form has spread throughout the entire country. From 1979 to 1982, 872 Chinese-foreign transactions were concluded in the form of compensation trade, involving total foreign capital of \$413 million, and with each transaction involving \$500,000 or less.¹⁵⁰ A more updated statistical figure shows that by the end of June 1987, \$2,500 million had been contracted in the form of

145. Consolidated Tax Regulations, *infra* note 349.

146. For a discussion of the CNOOC Model Contract, see Moser, *Legal Aspects of Offshore Oil and Gas Exploration and Development in China*, in FOREIGN TRADE, INVESTMENT, AND THE LAW IN THE P.R.C., *supra* note 70, 270, 277-83.

147. Nee, *supra* note 129, at 25-26.

148. Torbert & Thompson, *supra* note 101, at 822.

149. Moser, *supra* note 70, at 94.

150. See *China's Utilization of Foreign Capital, 1979-1982*, INTERTRADE, Oct. 1983, at 68.

compensation trade, processing and assembling transactions and international leases, and \$1,825 of these (73%) have been put to effective use.¹⁵¹

Under a compensation trade arrangement, the Chinese partner purchases or leases manufacturing equipment and/or technology from foreign firms. In return, the foreign firm receives payment either in kind or through goods produced as a direct result of the provisions of such equipments and/or technology.

Another form of the compensation trade arrangement that is used in the P.R.C. is the "indirect compensation trade agreement" or "counterpurchase agreement."¹⁵² Under this arrangement, part of the purchase price is repaid to the foreign partners who provide equipment and/or technology, through periodic shipments of exports which are unrelated to the equipment or technology provided by the foreign partner. The contract for compensation trade arrangement usually provides for the value of the purchase price and the interest rate which is added to the installment repayments. Interest is also to be paid in kind. There is no formal joint management structure under this arrangement, and each party to the contract is accountable for its profits and losses.¹⁵³

There are distinct advantages to using the compensation trade arrangement. It is an inexpensive and efficient method of obtaining simple subcontract work for the production of component parts and materials. One of the most attractive aspects of the compensation trade arrangement is that it has not been subjected to taxation either under the Joint Venture Income Tax Law or the Foreign Enterprise Income Tax Law.¹⁵⁴

Also, the lack of specific legislation gives the contractors a greater degree of flexibility. However, this does not mean that the parties to such transactions are not subject to any regulation under Chinese law. Certain Chinese laws and regulations in the field of foreign economic relations have a definite impact upon certain aspects of these transactions. For example, foreign exchange earned by the Chinese partner in hybrid arrangements involving processing and assembly operations is subject to the Interim Regulations on Foreign Exchange Control issued by the State Council in December 1980¹⁵⁵ and the Detailed Rules for Foreign Exchange Control of 1983.¹⁵⁶

151. See *supra* notes 13-16 and accompanying text.

152. Wilson, *supra* note 30, at 6.

153. See Moser, *supra* note 70, at 94, 95.

154. Nee, *supra* note 129, at 27.

155. Foreign Exchange Control Regulations, *supra* note 55, art. 9.

156. See 1983 Enterprise Foreign Exchange Control Rules, *infra* note 434.

6.3. Wholly Foreign-Owned Enterprises

Wholly foreign-owned enterprises first appeared in the P.R.C. in 1973 in the experimental special economic zone of Guangdong,¹⁵⁷ and were formally recognized in 1980 when the three SEZs in Guangdong Province officially came into being. The first legislative document to address this new form of investment was the 1980 Regulations on Special Economic Zones which expressly permitted foreign investors to establish such enterprises in the Guangdong SEZs.¹⁵⁸

Since 1984, special policies have been announced concerning the 14 coastal open cities¹⁵⁹ and certain major inland municipalities¹⁶⁰ which allow them to enjoy a special economic status. The Wholly Foreign-Owned Enterprise Law of 1986¹⁶¹ marked the beginning of the nation-wide legalization of wholly foreign-owned enterprises in the P.R.C. The law provides basic rules for the erection and operation of such entities. Foreign entrepreneurs are permitted to set up businesses independently with their own capital, especially in cities which have been designated centers for foreign investment.¹⁶² The profits and losses of wholly foreign-owned enterprises are free from restraint by the Chinese administrative system except as they are specifically regulated by law.¹⁶³ Chinese contractors may still provide the foreign-owned enterprises with land, factory buildings and raw materials at negotiated prices in foreign exchange. In return, the enterprises pay wages and welfare expenses to Chinese workers and administrative personnel as

157. See Stein, *Wholly Foreign-Owned Ventures in China: A Comparison of 3M China Ltd., Grace China Ltd. and The New Solely Foreign-Invested Enterprise Law*, 4 CHINA L. REP. 1, 3 (1987).

158. Regulations of the People's Republic of China on Special Economic Zones in Guangdong Province, *approved* August 26, 1980 by the Fifteenth Session of the Standing Committee of the Fifth National People's Congress, art. 1 (encouraging foreign investors to open factories or to set up enterprises and other establishments with their own investment or to undertake joint ventures with Chinese investment in the special economic zones), art. 10 (providing that foreign investors can operate their business independently in the special economic zones and employ foreign personnel for technical and administrative work), *reprinted and translated in* 5 CCH CHINA LAWS, *supra* note 18, at ¶ 70-800; FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 193, 201 [hereinafter SEZ Regulations].

It is said that, in theory, a wholly foreign-owned enterprise could have been established under the Joint Venture Law because while merely providing for a minimum amount of foreign investment at 25%, that law failed to establish a ceiling for the amount of foreign investment. This enables a foreign investor to become a 100% owner of a joint venture. See *id.*, art. 4. See also Stein, *supra* note 157, at 10.

159. See *supra* note 9.

160. See *supra* note 10.

161. Wholly Foreign-Owned Enterprise Law, *supra* note 37.

162. *Id.*, art. 2.

163. *Id.*, art. 11.

provided for by contract.¹⁶⁴

There is criticism that the Wholly Foreign-Owned Enterprise Law is silent and ambiguous on certain matters and leaves many questions unanswered.¹⁶⁵ For example, it is allegedly unclear whether a wholly foreign-owned enterprise established in the P.R.C. is a legal entity with an identity separate from its parent organization located outside the country. This question need not be answered by Chinese law. How a newly created foreign business is linked to its parent institution abroad is primarily a matter which is most appropriately left to the foreign jurisdiction's consideration. However, one obvious exception is that an enterprise based in the P.R.C. exclusively supported by foreign capital is not treated as a branch of its parent organization. The 1986 Law provides that "[e]nterprises with sole foreign investment as referred to in this Law are those enterprises established within Chinese territory, in accordance with the relevant Chinese laws, with capital provided totally by the foreign investor. [They do] not include branches in China of foreign enterprises or other economic organizations."¹⁶⁶

A question which does arise is whether the enterprises are Chinese corporations. This is addressed by a provision in the 1986 Wholly Foreign-Owned Enterprise Law which indicates: "[a]n enterprise with sole foreign investment which conforms to the conditions for becoming a legal person under the relevant Chinese regulations shall obtain such status in accordance with the law."¹⁶⁷ However, one could argue that if an established wholly-owned foreign enterprise does not meet the conditions as prescribed by Chinese law, it would not be treated as a legal person. What, then, would be its legal status under Chinese law? Theoretically, it could be a legal person without Chinese status. In actual practice, it is only the case for branches of foreign companies which are located in the P.R.C. The 1986 Wholly Foreign-Owned Enterprise Law explicitly excludes foreign branches from its scope of application.¹⁶⁸ In practice, when a wholly foreign-owned enterprise is approved and registered with the appropriate Chinese authorities, it automatically becomes a Chinese "citizen" because the Chinese authorities are unlikely to approve any proposal for a foreign enterprise which does not possess the characteristics required in order to be considered a Chinese corporation. Under the General Principles of Civil Law

164. *Id.*, art. 13.

165. Horsley, *Investing in China in 1987 and Beyond*, in *LEGAL ASPECTS OF DOING BUSINESS WITH CHINA* 59, 80-81 (1986) [hereinafter Horsley, *Investing in China*].

166. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 25.

167. *Id.*, art. 8.

168. *Id.*, art. 2.

promulgated on April 12, 1986, an enterprise must meet four general requirements: (1) it must be established in accordance with the law; (2) it must possess the necessary funds or other species of property; (3) it must have its own name, organizational structure and premises; and (4) it must be capable of independently bearing civil liability.¹⁶⁹ In addition to these requirements, foreign enterprises must meet requirements in approval and registration procedures.¹⁷⁰ While the Wholly Foreign-Owned Enterprise Law contains no detailed provisions regarding the application and registration procedures (a gap to be filled by a set of implementing regulations in the future), there are local stipulations regarding this.¹⁷¹

There are certainly incentives for the P.R.C. to allow foreign entrepreneurs to set up and operate enterprises in the P.R.C. First, since all the necessary funds are provided by the foreign investors, the Chinese need not worry about the financing or bear economic risks for the wholly foreign-owned enterprises. Second, because of the foreign investors' independent control of the enterprises, they are in a position to help the Chinese absorb and familiarize themselves with advanced technological and managerial skills. The task of getting a foreign enterprise to introduce its technological know-how would require little effort by the Chinese. The incentive for the foreign party lies in the foreign enterprise itself. In order to make its products more competitive in the world market and to earn more profits, a wholly foreign-owned corporation will be more likely to adopt technology and equipment than other forms of direct investment. It must also update and renew, from time to time, its technology and equipment: "This is conducive to our learning advanced techniques and management experience so as to keep up with the developments of sciences and technology in the world."¹⁷² Third, as a by-product foreign enterprises in the P.R.C. may assist

169. General Principles of Civil Law, *supra* note 43, ch. III, art. 37.

170. *Id.*, ch. III, art. 41. ("[E]nterprises with sole foreign investment established within Chinese territory which fulfil the conditions of a legal person shall acquire the status of a Chinese corporation following examination, approval and registration according to the law by the industrial and commercial administrative authorities.") But see Horsley, *Investing in China*, *supra* note 165, at 81. Even though a wholly-foreign owned business qualifies as a Chinese legal person, doubt still remains as to "whether it will be treated as a Chinese company or as a foreign enterprise within the Chinese regulatory scheme." *Id.*

Being a Chinese legal person or corporation is not the same as being a China-owned company. The uniqueness of being "wholly foreign-owned" is illustrative of the nature of a China-based foreign enterprise which, under Chinese law, enjoys both the status of a Chinese legal person and the privilege of independence.

171. See, e.g., Shanghai Trial Establishment Measures, *infra* note 179.

172. Liu, *Foreign Enterprises in Shenzhen Special Economic Zone*, in 1984 AL-MANAC, *supra* note 35, at 651.

with the training of Chinese technicians and workers. In fact, the technical skills required in a foreign enterprise are usually higher and stricter than those in a Chinese competitor. Foreign enterprises which hire Chinese personnel and workers through its planned training and manufacturing programs will transfer its more advanced techniques and skills to its Chinese employees. Those who have been employed in wholly foreign-owned enterprises are considered by the Chinese to be more experienced and skillful than their counterparts who work in purely Chinese-run enterprises. Fourth, foreign enterprises may increase employment opportunities for the local people. Finally, the Chinese Government may benefit by levying taxes upon wholly foreign-owned enterprises.¹⁷³

There are also incentives for foreign enterprises to establish operations in the P.R.C. For instance, wholly foreign-owned enterprises are free from Chinese administrative interference. The issue of profit-sharing never arises and they are free to adopt any method of management that best serves the achievement of their goals. Moreover, a wholly foreign-owned venture is free from the possibility of nationalization or expropriation by the Chinese government except where it is "necessary."¹⁷⁴ Where expropriation is deemed necessary, legal procedures will be followed and the appropriate compensation will be made. The P.R.C. has signed a number of investment protection agreements setting out the standards for compensation in cases of expropriation.¹⁷⁵

7. FOREIGN INVESTMENT ENTERPRISES: FORMATION AND OPERATION

7.1. Procedure for Establishment

7.1.1. Application

7.1.1.1. Project Proposals and Preliminary Feasibility Study Reports

7.1.1.1.1. *Equity and Contractual Joint Ventures.* In seeking to establish an equity joint venture or a contractual enterprise in the P.R.C., the initial step towards formal recognition is to submit project proposals

173. *Id.* See also Hou, *Xiang Challenges Draft Solely Foreign-Invested Enterprise Law*, Ta Kung Pao, Apr. 10-16, 1986, at 1.

174. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 5.

175. For a further discussion of wholly foreign-owned enterprises in the P.R.C., see Zhou, *A Comparative Study of Three Kinds of Enterprise Involving Foreign Investment in China*, in LEGAL ASPECTS OF FOREIGN INVESTMENT IN THE P.R.C. 110, 115 (1988); Jiang, *Some Theoretical Problems Related to the Legislation of Wholly Foreign-Owned Enterprises*, *id.* at 70.

to the appropriate governmental branch for examination and approval. Before this, a potential foreign investor needs to find an appropriate Chinese partner or co-operator. This may be arranged through either CITIC or the national and local foreign trading corporations, or CCPIT or the Ministries, local governments or individual local enterprises. Procedurally, the foreign investor may begin by contacting the Chinese partners through the mail or other means of communication in order to state its opinions concerning the proposed project, including the name, site, products to be manufactured, scope of production, amount of investment, extent of each side's contribution, form of investment, form of cooperation, distribution of profits, sources of capital, sources of raw materials, quality of the product and marketing channels. Once the connection has been established, the foreign investor may ask the Chinese partner(s) to submit a project proposal and a preliminary feasibility study report to the department directly in charge, provided that both sides have agreed on matters of consequence. Upon examination and consent by the department in charge, the project proposal and preliminary study report is submitted to the relevant foreign investment examining and approving body for approval.¹⁷⁶

7.1.1.1.2. Wholly Foreign-Owned Enterprises. No uniform form of application is yet readily available for wholly foreign-owned enterprises, but MOFERT has been working on this issue for several years. The 1986 Wholly Foreign-Owned Enterprise Law does not provide details concerning the application procedure for wholly foreign-invested projects. However, that issue will be addressed in the Detailed Rules and Regulations for Implementing the Wholly Foreign-Owned Enterprise Law which is currently awaiting approval.¹⁷⁷ Under the current practice in Shanghai, a potential foreign investor may rely on a national or local trust and investment corporation, a development corporation or a similar economic organization to process the application. The Chinese company or organization will then introduce the applicable national and local laws and regulations to the foreign investor, and refer him to the proper department for negotiations.¹⁷⁸ The proposal is then

176. For relevant provisions, see Joint Venture Law Implementation Regulations, *supra* note 52, ch. II, arts. 8-18.

177. See Moser, *supra* note 70, at 127.

178. The "proper department" denotes the department directly in charge of the same industry or trade in which the foreign investment project is planning to engage.
<https://scholarship.law.upenn.edu/jil/vol10/iss3/4>

submitted to an upper-level authority for approval.¹⁷⁹

7.1.1.2. *Examining and Approving Authorities; Initial Approval*

7.1.1.2.1. *Equity and Contractual Joint Ventures.* The project proposal and preliminary study reports for joint ventures are submitted to the relevant foreign investment examining and approving body for preliminary approval after they have been examined by the department in charge. The approving body is usually either the MOFERT or an entrusted provincial government (such as the COFERT) or an entrusted ministry or bureau operating under the State Council.¹⁸⁰ The appropriate authorities will then decide whether the project will conform with the state or local development goals and whether co-management conditions are ideal. After initial approval by the appropriate examining and approving body, the Chinese partner will invite the foreign investor to the P.R.C. for an on-site inspection of the potential investment environment and to sign a non-binding letter of intent for further negotiations.

The examining and approving bodies have different powers at different levels and places. For example, the bodies in Tianjin and Shanghai may approve projects involving investments of up to \$30 million as well as any nonproductive projects. Guangdong, Fujian, Beijing, Liaoning, Dalian, Guangzhou and Shenyang however, may only approve projects of up to \$10 million each. The other provinces, autonomous regions, coastal open cities and ministries under the State Council may approve projects of up to \$5 million each. Projects involving higher amounts of capital investment need to be examined and approved by the MOFERT.¹⁸¹ Also, if the local government or ministry does not possess the authority to approve a proposed project which involves a greater investment, it must transfer the project to the MOFERT.

The examining and approving body for wholly foreign-owned enterprises shall be "the State Council department in charge of foreign economic relations and trade or a body authorized by the State Council."¹⁸² To date, except in the SEZs and possibly in Shanghai, the State Council has not authorized a body other than the MOFERT to engage

179. See Regulations of Shanghai on Discussion and Examination and Approval Procedures Concerning the Establishment of Sino-Foreign Joint Equity Ventures and the Acceptance of Self-Operated Enterprises Invested in and Established by Foreign Business (Trial Implementation), issued by the Shanghai Municipal People's Government on July 1, 1984 art. 6, reprinted and translated in 5 CCH CHINA LAWS, *supra* note 18, at ¶ 91-008 [hereinafter Shanghai Trial Establishment Measures].

180. Joint Venture Law Implementation Regulations, *supra* note 52, arts. 8-9; Co-Operative Enterprise Law, *supra* note 38, art. 5.

181. Yue, *The ABC of Investing in China (IV): Application Procedure*, BEIJING REVIEW, June 15, 1987, at 26 [hereinafter Yue, *The ABC of Investing in China (IV)*].

182. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 6.

in examining and approving wholly foreign-owned enterprise applications. All applications should be filed with MOFERT.¹⁸³

7.1.1.3. *Negotiation; Formal Feasibility Study Reports*

7.1.1.3.1. *Equity and Non-Equity Joint Ventures.* Based on the principles set forth in the project proposals, both partners involved in a joint venture should study the letter of intent and investigate and discuss the details incorporated in the preliminary feasibility study report. Thereafter, both negotiating parties, only one party if so agreed upon or an entrusted consulting organ will write the formal feasibility study report. The study report should describe all the technical aspects of the proposed project as well as predict future costs and profits.¹⁸⁴ Any operating expenses likely to be incurred should be considered, including matters such as tax concessions or tax holidays, reduced customs duties on imports, favored treatment as to the pricing of local raw materials and utilities and land use costs. When necessary, the foreign investor could be asked to further inspect problems in order to avoid future disagreements. It is suggested that the foreign investor should double-check the infrastructural facilities in the area where the proposed venture is to be located, including the energy supply, transport facilities and source of raw and/or semi-finished materials, and "should not accept blindly everything the local officials claim."¹⁸⁵ In addition, the contracting parties should discuss the employment of local technicians and management personnel, and the ratio of the labor service fees proposed by the Chinese party to the expected productivity of the employees in their negotiations. In this situation, the Chinese partner is usually in a better position to secure approval for the formal feasibility study report from the appropriate authorities before submitting it to the governmental organ responsible for final approval and confirmation.¹⁸⁶

7.1.1.3.2. *Wholly Foreign-Owned Enterprises.* In the case of wholly foreign-invested project applications, once initial approval has been granted by the proper upper-level authority, the Chinese company assists with that department in more substantive negotiations with the foreign investor. Legal assistance from attorneys or legal experts must be obtained in order to ensure careful negotiation of the contract and articles of association. During negotiations, important issues relating to

183. See Nee, *supra* note 129, at 31.

184. See Yue, *The ABC of Investing in China (IV)*, *supra* note 181 at 25.

185. *Id.*

186. See generally Lubman, *Negotiation of Joint Venture Contracts* in LEGAL ASPECTS OF DOING BUSINESS WITH CHINA 787 (1986).

building facilities, land use, employment, production, sources of raw materials, and supplies, channels of sales and co-operation are customarily discussed and finalized.¹⁸⁷

7.1.2. *Final Approval*

7.1.2.1. *Joint Ventures and Co-Operative Enterprises.* After negotiations have been concluded, the contract and articles of association are submitted to the relevant government organ for final approval and confirmation. At this stage, the following items are submitted to the examining and approving body: the signed contract, articles of association, legal documents, the application for the establishment of the project, the final feasibility study report, and the names of candidates for the president, vice-presidents and other members of the board of directors. Any comments submitted by the department in charge and the provincial government must be attached with the proposal of the projected venture.¹⁸⁸ The approving and examining body shall then make a decision as to whether or not it will grant its approval within three (3) months or, in the case of contractual joint ventures, within 45 days, upon receipt of the application documents.¹⁸⁹ If the examination and approval authority finds improprieties or errors in the application documents, it will request that an amendment be made and submitted within a specified period of time. Approval will not be granted until the amendment is made.¹⁹⁰

7.1.2.2. *Wholly Foreign-Owned Enterprises.* As for wholly foreign-owned projects, the foreign investor may officially propose the investment plan and file the applications along with an opinion letter signed by both the proper department and the entrusted Chinese company, to the examining and approving body for the establishment of a wholly foreign-owned enterprise.¹⁹¹ To prevent undue delay, the decision must be made by the approving body within 90 days upon receipt of the official applications.¹⁹²

7.1.3. *Registration*

7.1.3.1. *Joint Ventures and Co-Operative Enterprises.* The Joint

187. Shanghai Trial Establishment Measures, *supra* note 179, art. 6.

188. Joint Venture Law Implementation Regulations, *supra* note 52, art. 9(2).

189. Co-Operative Enterprise Law, *supra* note 38, art. 5.

190. Joint Venture Law, *supra* note 36, art. 3; Joint Venture Law Implementation Regulations, *supra* note 52, art. 10.

191. Shanghai Trial Establishment Measures, *supra* note 179, art. 6.

192. The Wholly Foreign-Owned Enterprise Law provides:

Applications for establishment of enterprises with sole foreign investment

Venture Law requires all officially approved joint ventures to register with the State General Administration for Industry and Commerce (SAIC) in order to obtain a license to begin operations.¹⁹³ The SAIC may authorize local Administrative Bureaus for Industry and Commerce (ABIC) to register joint ventures in their localities. However, operating licenses shall not be issued until the local registration has been examined by the SAIC.¹⁹⁴ The corresponding language in the Joint Venture Law Implementation Regulations is somewhat different. Under these regulations, the joint venture must register with the "registration and administration office" which is not the SAIC itself, but "the administrative bureau for industry and commerce of the province, autonomous region or municipality directly under the central government" where the joint venture is located.¹⁹⁵ An application for registration must be made within one (1) month after receipt of the "certificate of approval" from the examining and approving authority.¹⁹⁶ The following items must be presented to the registration office by a joint venture applying for registration: 1) a document of approval (certificate); 2) the joint venture agreement; 3) the joint venture contract; 4) the articles of association of the joint venture; and 5) a duplicate of the license and document(s) issued by the appropriate government department(s) in the country or region from where the foreign participants in the joint venture come.¹⁹⁷ A joint venture is officially established on the date on which the registration and administration office issues the operating license.¹⁹⁸

7.1.3.2. Wholly Foreign-Owned Enterprises. The registration procedure for the wholly foreign-owned enterprise is similar. Once approval has been granted to a foreign investor seeking to establish a wholly foreign-owned enterprise, the Wholly Foreign Owned Enterprise Law requires that registration applications be made to the industrial and commercial administrative authorities within 30 days, upon receipt of the approval certificate.¹⁹⁹ These registration applications should

are submitted for examination and approval by the State Council department in charge of foreign economic relations and trade or a body authoris[sic] by the State Council. The examining and approving body shall, within 90 days of receipt of the application make a decision whether or not to approve the application.

Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 6.

193. Joint Venture Law, *supra* note 36, art. 3.

194. Joint Venture Registration Regulations, *supra* note 51, art. 2.

195. Joint Venture Law Implementation Regulations, *supra* note 52, art. 11.

196. Joint Venture Registration Regulations, *supra* note 51, art. 2.

197. *Id.*, art. 3.

198. *Id.*, art. 5.

199. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 7.

clearly specify the product[s] to be manufactured, the total investment and registered capital, the size of the site, the labor force required, the source of materials, and the proposed terms of operation and credit references.²⁰⁰ The Wholly Foreign-Owned Enterprise Law does not provide a deadline for the registration office, but under the Shanghai Trial Establishment Measures, industrial and commercial administration authorities are required to issue a business license within one month.²⁰¹ The wholly foreign-owned enterprise is considered to be established on the date the operating license is issued.²⁰² After issuance, the foreign investor must invest and establish itself in the P.R.C. within the time limit set by the examining and approving authority. Failure to do so will entitle the industrial and commercial administrative authorities to revoke the license.²⁰³ These authorities are also empowered to review and supervise the investment status of wholly foreign-owned enterprises.²⁰⁴

7.2. Capital Contributions

7.2.1. Joint Ventures

Contributions of capital under the Joint Venture Law are usually made in the form of cash, capital goods, or industrial property rights.²⁰⁵ Contributions in kind (capital goods) and in industrial property may include buildings, equipment or other materials, industrial property rights, know-how, or the right to land use. The prices for contributions in kind and industrial property (excluding the right to land use) are to be ascertained through consultation by the parties involved or through evaluation by an approved third party.²⁰⁶

Generally, the proportion of the foreign partner's contribution must not be less than 25% in the registered capital of a joint venture.²⁰⁷ The parties to the venture share the profits, risks, and losses according to the ratio of the mutually agreed capital contribution values.²⁰⁸ Also, joint venture partners are issued "investment certificates" rather than shares of stock.²⁰⁹ Under a recent promulgation,²¹⁰ the registered capi-

200. Horsley, Investing in China, *supra* note 165, at 83.

201. Shanghai Trial Establishment Measures, *supra* note 179, art. 5.

202. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 7.

203. *Id.*, art. 9.

204. *Id.*

205. Joint Venture Law, *supra* note 36, art. 5.

206. Joint Venture Law Implementation Regulations, *supra* note 52, art. 25.

207. Joint Venture Law, *supra* note 36, art. 4(2).

208. *Id.*, arts. 4, 5; Joint Venture Law Implementation Regulations, *supra* note 52, art. 25.

209. With the exception of the recently restored Shanghai Stock Exchange for
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tal of a joint venture is restricted, depending on the amount of the total investment.

More recently, the Ministry of Foreign Economic Relations and Trade (MOFERT) and the SAIC co-issued a set of provisions,²¹¹ the Several Provisions on Capital Contributions to Sino-Foreign Equity Joint Ventures by Each of the Joint Venturers, regulating the capital contributions by the individual parties to a joint venture enterprise. According to Article 4, where the joint venture contract requires the parties to make total lump-sum contributions at once, they must do so within six (6) months after the date on which the venture's business license is issued. If periodic payments are called for in the contract, the parties must make payments for the first period within three (3) months of the operating license's issuance. Payments for this period may not be less than fifteen percent of the total investment each partner has contracted to contribute to the project.²¹² If the parties fail to provide capital contributions to the joint venture in accordance with Article 4 the joint venture is automatically dissolved, and the certificate of approval ceases to be effective.²¹³ These provisions became effective on March 1, 1988.

7.2.2. Co-Operative Enterprises

Under the newly promulgated Co-Operative Enterprise Law, the

trial use, and the securities exchange markets in Shenyang, Shanghai and Guangzhou, there is no extensive stock market in China. See *Securities Exchange Business Opened in Guangzhou*, People's Daily, Nov. 10, 1987, at 1.

210. Provisional Regulations of the State Administration for Industry and Commerce on the Ratio Between the Registered Capital and Total Investment of Sino-Foreign Joint Equity Enterprises, promulgated by the State Administration for Industry and Commerce on Mar. 1, 1987, art. 3, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-554. For instance, the registered capital of a joint venture must amount to at least 70% of the venture's total investment if the total investment is three million dollars or less. If the total is between three and ten million dollars, the registered capital must not be less than 50% of the total, provided that where the total investment is less than \$4.2 million, the registered capital may not be less than \$2.1 million. Where the total investment ranges from \$10 million to \$30 million, the capital registered may not be less than 40% of the total investment, provided that the registered capital may not be less than \$5 million if the total investment is less than \$12.5 million. Where the total investment exceeds \$30 million, the registered capital must be at least one-third of the total, provided that the capital may not be less than \$12 million if the total investment is less than \$36 million.

211. *Zhongwai Hezi Qiye Heying Gefang Chuizi de Ruogan Guiding* [Several Provisions on Capital Contributions to Sino-Foreign Equity Joint Ventures by Each of the Joint Venturers], *approved by* the State Council on Dec. 30, 1987 *promulgated by* the MOFERT and the SAIC on Jan. 1, 1988, *reprinted in* People's Daily, Jan. 15, 1988, at 3.

212. *Id.*, art. 4.

213. *Id.*, art. 5.

capital investment and/or conditions for co-operation established by both Chinese and foreign parties may be in the form of cash, kind, land-use rights, industrial property rights, non-patented technology or other property rights.²¹⁴ According to current practices, contractual joint venture contributions may also include labor services.²¹⁵ The profits and losses shared can be different from the ratio of capital contributions between the parties, and such contributions, risk sharing and distribution are established in the co-operative enterprise contract by the co-operating parties.²¹⁶ Under certain circumstances, the capital can be returned to the parties during the term of the enterprise's operation, but the returned capital is subject to recall where losses result.²¹⁷ Both parties are thus clearly expected to duly fulfill their obligations of contributing the full investment amount and providing the conditions for co-operation. Failure to provide such contributions within the time limit set forth in the co-operative enterprise contract may result in an action by the administration of industry and commerce to establish a deadline for fulfillment. If the obligations are still not fulfilled by the new deadline, the examination and approval authority and the administrative authorities for industry and commerce may take further actions in accordance with relevant state provisions.²¹⁸

7.2.3. Wholly Foreign-Owned Enterprises

The present regulations do not establish an amount or minimum amount a foreign company must invest in its wholly-owned P.R.C. subsidiary. By definition, a wholly foreign-owned enterprise is capitalized solely by the foreign parent or affiliate company; everything necessary for the establishment and operation of its business rests upon the foreign investor. However, there are several points which deserve mention. First, it is the MOFERT's intention that the letter of application for establishing a wholly foreign-owned enterprise should include, among other things, the total amount of the investment or the registered capital and the investment implementation plan.²¹⁹ Second, in order to qualify as a Chinese corporation, the wholly foreign-owned enterprise must possess adequate assets or funds.²²⁰ Generally, the enterprise's liability is limited to its assets and does not extend to other assets of the parent

214. Co-Operative Enterprise Law, *supra* note 38, art. 8.

215. See Nee, *supra* note 129, at 26, 27.

216. Co-Operative Enterprise Law, *supra* note 38, arts. 2, 22.

217. *Id.*, art. 22.

218. *Id.*, art. 9.

219. See Moser, *supra* note 70, at 128.

220. General Principles of Civil Law, *supra* note 43, art. 37.

investor.²²¹ Theoretically, however, undercapitalization may enable a Chinese court to "pierce the corporate veil," by extending the liability of the undercapitalized enterprise to the assets of its foreign investor(s). Third, a wholly foreign-owned enterprise is under statutory obligation to adopt advanced technology and equipment (or to export all or most of its products), and to establish itself within a time limit specified by the registration authorities,²²² though it is not clear at this stage what the consequence is if the enterprise fails to provide adequate capital or assets for its establishment within the specified time limit.

7.3. *Operational Matters*

7.3.1. *Joint Ventures*

Joint ventures are managed by a Board of Directors, whose composition must be specified in the joint venture contract and the articles of association.²²³ The chairperson or the president of the Board must be appointed by the Chinese joint venturer, and the vice-chairperson(s) appointed by the foreign participant(s).²²⁴

The board of directors is the highest authority of the joint enterprise, and has the power to rule on all important matters concerning the joint venture.²²⁵ These matters include expansion projects, production and business programs, the budget, the distribution of profits, labor force and payment plans, the termination of business, the appointment or hiring of the president and vice-president(s) of the joint venture (not that of the Board itself), the chief engineer and the treasurer and auditors, as well as their functions, powers and remuneration.²²⁶ The joint venture is responsible for establishing the management and operation plans in accordance with the guidelines regarding the scope of operation and scale of production stipulated in the joint venture contract. The joint venture has the right to purchase the necessary machinery, equipment, raw materials, fuel, components, means of transport and other materials either in the P.R.C. or abroad. However,

221. *Id.*, art. 48.

222. *See* Wholly Foreign-Owned Enterprise Law, *supra* note 37, arts. 3, 9.

223. Joint Venture Law Implementation Regulations, *supra* note 52, arts. 14, 16.

224. *Id.* art. 34; Joint Venture Law, *supra* note 36, art. 6; The Chinese party may appoint a foreign citizen as the chairperson or president of the Board, although it is highly unlikely. However, some Chinese state-owned enterprises, such as a large and well-known big machinery factory in Wuhan whose general manager is a West German, have invited and appointed foreign nationals as their primary managers or directors.

225. Joint Venture Law Implementation Regulations, *supra* note 52, art. 33.

226. Joint Venture Law, *supra* note 36, art. 16.

priority should be given to purchasing raw materials and supplies in the P.R.C. whenever possible.²²⁷

7.3.2. *Co-Operative Enterprises*

Co-operative enterprises having the status of a legal person also have a board of directors management system. These enterprises closely follow the provisions for equity joint ventures found in the Joint Venture Law Implementation Regulations. For forms of contractual joint ventures where no novel legal entity is formed and no common board of directors exists, however, the management structure is more flexible and the majority of important matters are to be determined and approved by both parties either through regularly held meetings of representatives from both sides or through a joint committee.²²⁸ Joint committees and joint meetings are necessary to maintain contact between the parties and to scrutinize their respective efforts to realize the project goals. One of the parties may be appointed to manage the routine business operations of the enterprise. Day-to-day management matters are usually stipulated in a separate management contract in addition to the basic co-operation contract (the venture contract), though both contracts are subject to the same authority's examination and approval.²²⁹ The new Co-Operative Enterprise Law seems to reflect this practice in that a contractual joint venture may either establish a board of directors or a joint managerial body similar to the joint committee arrangement. Either establishment may decide on the appointment or employment of a general manager who will assume full responsibility of the routine operation and management of the enterprise, and who shall report to the board or joint managerial body.²³⁰

7.3.3. *Wholly Foreign-Owned Enterprises*

A wholly foreign-owned enterprise is permitted to carry out its operation and management in accordance with the enterprise's approved articles of association without interference from the Chinese government. However, the enterprise must operate under the auspices and with the assistance of local Chinese governmental authorities. The enterprise's production and operating plans must be filed with the proper authorities.²³¹ Local FTCs, especially trust and investment cor-

227. Joint Venture Law Implementation Regulations, *supra* note 52, art. 57.

228. *See Nec*, *supra* note 129, at 28.

229. *Id.*

230. Co-Operative Enterprise Law, *supra* note 38, art. 12.

231. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 11.

porations, consulting companies and municipal authorities, are often involved not only in assisting foreign investors to register and obtain approval but also in regard to operations.

7.4. Labor Relations

7.4.1. Joint Ventures

As for equity joint ventures, the conditions for the employment and discharge of workers and personnel must be carried out in accordance with the provisions of the joint venture agreement.²³²

Chapters XII and XIII of the Joint Venture Law Implementation Regulations, respectively subtitled "Staff and Workers" and "Trade Unions," provide detailed guidelines for labor relations in Sino-foreign joint ventures. For instance, Article 92 requires joint ventures to make efforts to provide professional and technical training for their staff and workers and to establish a strict examination system in order to meet the requirements of production and managerial skills, while Article 93 clearly establishes that the payment of salaries must be according to one's work and that there should be more pay for more work.²³³ Staff members and workers are entitled to set up trade union organizations, and such unions have the power to represent the staff and workers to sign labor contracts with the joint venture and to supervise the implementation of such contracts. The representatives of trade unions also have the right to participate as non-voting members and to report the opinions and demands of staff and workers to the meetings of the board of directors when the board discusses important matters relating to development plans, production and operation and other similar activities.²³⁴ As for employment, recruitment, discharge resignation, salary, welfare benefits and other matters relating to the staff and workers, the Implementation Regulations refer to the 1980 Joint Venture Labour Management Regulations.²³⁵

The Labour Management Regulations extensively amplified and corrected the 1979 Joint Venture Law by mandating the use of labor contracts²³⁶ and stipulating minimum salaries²³⁷ and conditions and procedures for employment, dismissal, and resignation of workers.²³⁸

232. Joint Venture Law, *supra* note 36, art. 6 (4).

233. Joint Venture Law Implementation Regulations, *supra* note 52, arts. 92, 93.

234. *Id.*, arts. 95, 96, 98.

235. *Id.*, art. 91.

236. Joint Venture Labor Management Provisions, *supra* note 53, art. 2.

237. *Id.*, arts. 8, 9.

238. *Id.*, arts. 3-7.

The labor contract should provide for matters pertaining to the following: employment, dismissal, working hours, production and other tasks, salaries, awards and punishments, vocations, insurance and welfare, labor protection, and labor disciplines. With the exception of small joint ventures which may sign labor contracts with employees on an individual basis, labor contracts generally are signed collectively by the trade union and the joint venture. All signed labor contracts are to be approved by the local labour management department.²³⁹ Workers and personnel are recommended by either the local department in charge of the joint venture or the local labor management department, or, such persons are directly recruited by the joint venture with the consent of the local labor management department. Merit is the basis for employment. Qualifications of employee candidates are evaluated by examinations.²⁴⁰ The joint venture may, in accordance with the terms of the labour contract, dismiss employees who become less productive as a result of changes in production and technical conditions, and who fail to meet the requirements established by the joint venture after training and are not suitable for other work. However, compensation must be made to discharged staff and workers. The dismissed will be assigned to other work by the local department in charge of the joint venture or by the local labor management department.²⁴¹

Punitive actions are allowed against employees whose violations of the rules and regulations of the venture have resulted in "certain harmful consequences."²⁴² Dismissals are one method of punishment and must be reported to the local department in charge and the local labor management department. The trade union has the power to intervene and raise objections when it considers the dismissal or punishment by discharge unreasonable.²⁴³ Article 14 of the Labor Management Provisions provides that any labor dispute occurring in a joint venture shall first be settled through consultations by the parties involved in the dispute. If the dispute cannot be settled through consultations, the ag-

239. *Id.*, art. 2.

240. *Id.*, art. 3.

241. *Id.*, art. 4.

242. *Id.*, art. 5. The Labor Management Provisions do not explain what constitutes "certain" harmful consequences. In January 1984, the Ministry of Labor and Personnel issued a set of Measures for the Implementation of the Joint Venture Labor Management Provisions, *reprinted and translated in COMMERCIAL BUSINESS AND TRADE LAWS: PEOPLE'S REPUBLIC OF CHINA*, Bk. 3, 101 (1985). Clause (10) of the Measures provide that a joint venture may "take disciplinary actions against those workers and staff members who have violated the labor disciplines and the rules and regulations of the joint venture, which result in *unfavorable consequences*." (emphasis added).

243. Joint Venture Labor Management Provisions, *supra* note 53, arts. 5, 6.

grieved party, the other party, or both parties may request arbitration before the provincial or municipal labor management department. If any party objects to the arbitration award, he or she may initiate legal proceedings in a Chinese court.²⁴⁴

7.4.2. *Co-Operative Enterprises and Wholly Foreign-Owned Enterprises*

Except for Articles 13 and 14 of the Co-Operative Enterprise Law, and Articles 12 and 13 of the Wholly Foreign-Owned Enterprise Law, there are not yet any published laws and regulations governing labor relations in co-operative and wholly foreign-owned enterprises. However, such matters may be dealt with in the co-operation agreement or in the articles of association of the foreign-owned enterprise. The guidelines set forth for equity joint ventures are basically applicable to non-equity joint venture enterprises "by reference."²⁴⁵ The Co-Operative Enterprise Law provides that the employment, dismissal, remuneration, welfare, labor protection, and labor insurance of the workers and staff members of a co-operative enterprise "shall be stipulated in contracts signed in accordance with the law."²⁴⁶ In addition, employees of the enterprise shall, in accordance with law, establish their trade union organization to carry out union activities and protect their lawful rights and interests, and the enterprise, in turn, shall provide the trade union with the necessary conditions for its activities.²⁴⁷ While the Law does not specify in what type of "contracts" the labor-related terms should be set out in, one may interpret the language of the Law to include both the co-operative enterprise contract and labor contracts.

A look at the relevant provisions in the Wholly Foreign-Owned Enterprise Law reveals its similarity to the Co-Operative Enterprise Law. Under the Wholly Foreign-Owned Enterprise Law, a wholly foreign-owned enterprise employing Chinese staff and workers must sign labor contracts in accordance with the law.²⁴⁸ The contract must make clear matters relating to employment, dismissal, remuneration, welfare, labor protection and labor insurance.²⁴⁹ The employees of a wholly foreign-owned enterprise may set up trade union organizations which un-

244. *Id.*, art. 14.

245. See Moser, *supra* note 70, at 98 ("In most of its day-to-day operations, a contractual joint venture is subject to the same types of regulations and restrictions regarding insurance . . . and labour management as are applicable to equity joint ventures.").

246. Co-Operative Enterprise Law, *supra* note 38, art. 13.

247. *Id.*, art. 14.

248. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 12.

249. *Id.*

dertake trade union activities and protect the rights and interests of the employees. The foreign-owned enterprise must provide the facilities for carrying out the trade union's activities.²⁵⁰ These provisions, though brief, essentially coincide with the provisions governing equity joint ventures.²⁵¹ As a result, it can be said that, until detailed rules are released to guide labor management in co-operative and wholly foreign-owned enterprises, the existing rules for joint ventures provide temporary guidelines for all three forms of foreign-invested enterprises.

8. TRANSFER OF TECHNOLOGY

Due to rapid developments in recent years, technology transfer to the P.R.C. has become a subject which has received a great deal of attention.²⁵² According to current Chinese practice, the transfer of technology (primarily imported technology), is made through either "pure technology licensing contracts," combined sales and licensing contracts, countertrade arrangements, or direct foreign investment transactions.²⁵³

As is the case with almost every other socialist country which is eager to gain access to foreign technology, the P.R.C. is more interested in combined arrangements involving not only sales or investment contracts but technology licensing agreements as well. Direct foreign investment arrangements are the most favored form of technology import to the Chinese. Indeed, one of the major purposes behind the P.R.C.'s absorption of foreign investment is to import more advanced foreign technology. Industrial property rights under Chinese law may be used as substantial parts of total foreign investment in a joint venture or contractual joint venture arrangement. Some points a foreign investor should keep in mind are: the legal protection available in the P.R.C. for industrial property rights, the basic legal framework for the P.R.C.'s internal and external technology transfer (especially import of technology), the statutory requirement concerning the quality of the technology imported, and sanctions for providing obsolete technology and equipment.

250. *Id.*, art. 13.

251. See *supra* notes 232-39 and accompanying text.

252. See generally PENDLETON, *INTELLECTUAL PROPERTY LAW IN THE PRC: A GUIDE TO PATENTS, TRADE MARKS AND TECHNOLOGY TRANSFER*; Kirk, *Chinese Intellectual Property and Technology Acquisition*, 13 *INTELL. PROP. L. REV.* 175 (1981); Lubman, *Trade Contracts and Technology Licensing*, *LEGAL ASPECTS OF DOING BUSINESS IN CHINA* 9-64; Thurston, *Technology Takes Command: the Policy of the People's Republic of China with respect to Technology Transfer and Protection of Intellectual Property*, 21 *INT'L LAW.* 129 (1987).

253. See Wilson *supra* note 236, at 3-8.

8.1. Trademarks

8.1.1. Applicable Laws

The Chinese trademark protection system is the first among patent and other intellectual property rights in recent years to be updated. To date, the major governing laws and regulations in this area are the following: 1) the 1982 Trademark Law;²⁵⁴ 2) the 1985 Priority Trademark Registration Regulations;²⁵⁵ 3) the 1985 Trademark Reproduction Measures;²⁵⁶ and 4) the 1988 Trademark Rules.²⁵⁷ The 1982 Trademark Law, which supersedes the Regulations on Trademark Administration of April 10, 1963, is the most important trademark legislation. It regulates the application process for trademark registration, examination and approval of trademark registration, renewal, assignment and licensing of registered trademarks, trademark-related dispute settlement, the administrative control of the use of trademarks, and protection of the exclusive right to registered trademarks. The 1988 Trademark Rules, which can be viewed as authorized official interpretations of the Trademark Law, provides for detailed procedures and measures for implementing the 1982 Trademark Law. The 1985 Priority Trademark Registration Regulations were issued to enforce the relevant provisions of the Paris Convention to which the P.R.C. acceded prior to the issuance of those regulations.²⁵⁸ The 1985 Trademark Reproduction Measures, which supersede the Regulations for the Administration of the Reproduction of Trademarks of March 23, 1983, were promulgated to implement the Trademark Law more effectively and to strengthen the administration of the reproduction of trademarks, to pro-

254. *Shang Biao Fa* [Trademark Law of the People's Republic of China], adopted by the Twenty-Fourth Session of the Standing Committee of the Fifth National People's Congress on Aug. 23, 1982, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 11-500 [hereinafter 1982 Trademark Law].

255. *Guanyu Shenqing Shangbiao Zhuze Yaoqiu Youxian Quan de Zanxing Guiding* [Provisional Regulations Governing Applications for Priority Registration of Trademarks in China], approved by the State Council, promulgated by the SAIC on Mar. 15, 1985, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 11-523 [hereinafter 1985 Priority Trademark Registration Regulations].

256. *Shangbiao Yinzhi Guanli Zanxing Banfa* [Provisional Measures for the Administration of the Reproduction of Trademarks], promulgated by the SAIC on Dec. 21, 1985, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 11-526 [hereinafter 1985 Trademark Reproduction Measures].

257. *Shang Biao Fa Shishi Xize* [Detailed Rules for the Implementation of the Trademark Law of the PRC], approved by the State Council on Jan. 8, 1988, promulgated by the SAIC on Mar. 10, 1983, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 11-520 [hereinafter 1988 Trademark Rules]. The 1988 Trademark Rules supersede a set of rules promulgated in 1983 to implement the 1982 Trademark Law.

258. Paris Convention, *supra* note 60.

tect the exclusive right of registered trademarks, and to guarantee the interests of consumers.

8.1.2. General Issues

The main purposes of the Trademark Law are to improve the administration of trademarks, to ensure trademark exclusivity, and to encourage producers to guarantee the product quality implied by their trademarks.²⁵⁹ Such guarantees can help to protect consumer interests and to develop the P.R.C.'s socialist commodity economy.

Trademarks in the P.R.C. are protected through registration. Service marks are not covered by the Trademark Law. Unregistered or unapproved trademarks are not protected.²⁶⁰ If a reciprocal agreement exists on the registration of trademarks between the P.R.C. and a foreign applicant's country, or if an international treaty to which both countries are parties exists, the protection is only available to the foreign applicant, and the trademark must have already been registered in the applicant's home country.²⁶¹ Nationals of the Paris Convention member countries may, after filing an application for a trademark in any other member country, file another application for priority registration of the same trademark for the same product in the P.R.C. within 6 months after the first filing according to Article 4 of the Paris Convention.²⁶² Foreign applicants for the registration of a trademark in the P.R.C. must entrust an organization designated by the State to act on their behalf.²⁶³

All applications for registration of trademarks are to be made to the Trademark Office which operates under the SAIC, and is empowered to either accept or reject trademark applications. The trademark protection exists for ten (10) years once the application is accepted and the trademark registered.²⁶⁴

A trademark is assignable upon approval by the SAIC²⁶⁵ and may be licensed upon the submission of licensing agreements to the Trademark Office.²⁶⁶ Trademark disputes are usually settled internally within the SAIC.²⁶⁷ However, false representation, violation of Article 8 (which contains certain prohibitions) and other varieties of deceptive

259. 1982 Trademark Law, *supra* note 254, art. 1.

260. *Id.*, art. 5.

261. *Id.*, art. 9.

262. 1985 Priority Trademark Registration Regulations, *supra* note 255, art. 2.

263. 1982 Trademark Law, *supra* note 254, art. 10.

264. *Id.*, arts. 2, 4, 23.

265. *Id.*, art. 25.

266. *Id.*, art. 26.

267. *Id.*, arts. 27, 29.

conduct, as well as any infringement of the exclusive rights to use the trademark, may be litigated in the courts.²⁶⁸

8.2. Copyright

There is not yet specific legislation on copyright protection in the P.R.C. The State has organized a Copyright Study Group to study the feasibility of promulgating a copyright law in the near future.²⁶⁹ Because the P.R.C. joined the World Intellectual Property Organization (WIPO), a body which administers both the Berne Convention for the Protection of Literary Works²⁷⁰ and the Universal Copyright Convention²⁷¹ in 1980, the process of preparation and legislation on copyright law is bound to accelerate.

Individual literary works as well as scientific and technological inventions have received very little protection in the past due primarily to ideological barriers.²⁷² Copies could be freely made in any manner as long as the original work could be obtained. The Chinese Government's attitude toward copyright and other industrial properties, has, however, changed fundamentally. Currently, there is open recognition of private rights in technology and other intellectual properties, as evidenced in the General Principles of Civil Law "[c]itizens and legal persons shall enjoy the right of authorship, and shall have the right to sign their names as authors, issue and publish their works and obtain remuneration in accordance with the law[.]"²⁷³ Further, "if the rights of authorship (copyright) . . . of citizens or legal persons are infringed upon by such means as plagiarism, modification or imitation, they shall have the right to demand that the infringement be stopped, its illegal effects be eliminated and the damage be compensated for."²⁷⁴ This increasing recognition of intellectual property rights may be further seen from the

268. *Id.*, arts. 34, 36, 39. For more in-depth treatment of China's trademark system, see Cheng & Liss, *Summary of Current Trademark Law and Practice in the People's Republic of China*, 82 PATENT & TRADEMARK REV. 505 (1984); Leung, *Trademark: Paris Convention Member Nationals Get Priority*, 7 E. ASIAN EXEC. REP., June 15, 1985, at 15.

269. See PENDLETON, *supra* note 252, at 39-40.

270. International Convention Relative to the Protection of Literary and Artistic Works, done at Berne, Sept. 9, 1886, 77 British and Foreign State Papers 22 (1885-1886), as revised at Berlin, Nov. 13, 1908, 1 L.N.T.S. (1920).

271. Universal Copyright Convention, Sept. 6, 1952, 6 U.S.T. 2731, T.I.A.S. No. 3324, 216 U.N.T.S. 133, as revised at Paris, July 24, 1971, 25 U.S.T. 1341, T.I.A.S. No. 7868 (entered into force July 10, 1974).

272. See Leung, *The Development of Intellectual and Industrial Property Law in China*, 1 ASIA PAC. COMM. L. 4, 6 (1984).

273. General Principles of Civil Law, *supra* note 43, art. 94.

274. *Id.* art. 99.

Trademark Law, the Patent Law,²⁷⁵ and the work of the Copyright Study Group. The opinion of a senior member of the Study Group reflects the Government's attitude and possibly its future policy on copyright protection:

(1) [W]e recognize that copyright is a type of property; (2) we recognized [sic] that copyright, generally speaking, is a type of right that may be owned by an individual; (3) we recognize that copyright is a type of exclusive right. . . ; (4) we will give adequate protection to both the moral and economic rights of the author; and (5) such rights of the author will be neither unduly wide, nor will they be too narrow to meet the requirements of the Universal Copyright Convention.²⁷⁶

He further indicated that, the P.R.C. will consider adhering to the Universal Copyright Convention (U.C.C.), that as the copyright laws currently stand, the scope of protection in the P.R.C. will not be more narrow than the minimum requirements of the U.C.C., and that "the level of protection in China must be higher than that provided in some other socialist countries."²⁷⁷

8.3. Patents

8.3.1. Applicable Laws

The patent system of the P.R.C. was first formulated in the 1950s. It was not until some thirty years later that the 1984 Patent Law,²⁷⁸ the first of its kind in the history of the P.R.C.'s, was finally enacted by the N.P.C. The Patent Law consists of 69 articles contained in eight chapters.²⁷⁹ Following the Patent Law's entry into force, the Patent Office issued the 1985 Patent Law Implementing Regulations,²⁸⁰ which

275. See *infra* note 278.

276. Zheng, *The Future Chinese Copyright System and Its Context*, 1984 INT'L REV. INDUS. PROP. & COPYRIGHT L. 141, 142-43 (1984).

277. *Id.*, at 155.

278. *Zhuanli Fa* [Patent Law of the People's Republic of China], *adopted by the Fourth Standing Committee of the Sixth National People's Congress on Mar. 12, 1984, reprinted and translated in 2 CCH CHINA LAWS, supra* note 18, at ¶ 11-600 [hereinafter 1984 Patent Law].

279. These chapters are subtitled "General Provisions," "Requirements for Grant of Patent Right," "Application for a Patent," "Examination and Approval of Application for Patent," "Duration, Cessation and Invalidation of Patent Right," "Compulsory License for Exploitation of the Patent," "Protection of Patent Right" and "Supplementary Provisions."

280. *Zhuanli Fa Shishi Xize* [Implementing Regulations of the Patent Law of the People's Republic of China], *approved by the State Council, promulgated by the*
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consists of 96 articles in 10 chapters. In order to facilitate the handling of the patent application and other patent-related matters (including patent assignment and licensing), the 1985 Patent Agencies Regulations²⁸¹ were subsequently promulgated to implement Articles 19 and 20 of the 1984 Patent Law concerning patent agencies. The General Principles of Civil Law of 1986 affirms that "[p]atent rights lawfully obtained by citizens and legal persons shall be protected by law."²⁸² All these legislative acts and promulgations provide the first full-range statutory protection for patent rights and inventions.

8.3.2. General Issues

The patent system of the P.R.C. can be traced back to the 1950 Provisional Regulations on the Protection of Invention Rights and Patent Rights.²⁸³ Those regulations were replaced several times, in 1954, 1963, and 1978. The 1978 Invention Regulations²⁸⁴ were amended in 1984 and remain effective in conjunction with the Patent Law. The 1978 Invention Award Regulations focus on what is considered to be significant new scientific and technological achievements which 1) must be *original* or have never been achieved before, 2) are more *advanced* than that which is currently available, and 3) are proved *useful* or *applicable* through actual practice.²⁸⁵ Under this law, the inventor enjoys

Patent Office of the People's Republic of China on Jan. 19, 1985, *reprinted and translated* in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 11-603 [hereinafter 1985 Patent Law Implementing Regulations]. The detailed stipulations which are provided in the 1985 Patent Law Implementing Regulations are: terms of patent application (Chapter II), examination and approval of such application (Chapter III), the invalidation of patent right (Chapter IV), compulsory licensing (Chapter V), rewards to inventors or creators of service or employment related inventions and creations (Chapter VI), patent administration authority (Chapter VII) and patent register and patent gazette (Chapter VIII).

281. *Zhuanli Daili Zanxing Guiding* [Provisional Regulations on Patent Agencies], *approved* by the State Council on Sept. 4, 1985 and *promulgated* by the Patent Office of the People's Republic of China on Sept. 12, 1985, *reprinted and translated* in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 11-609 [hereinafter 1985 Patent Agencies Regulations].

282. General Principles of Civil Law, *supra* note 43, art. 95.

283. *Faming Quan He Zhuanli Quan Baohu Zanxing Tiaoli* [Provisional Regulations on the Protection of the Invention Right and Patent Right], *promulgated* by the Administration Council in 1950 (no longer in force). See Moser & Ho, *The Registration and Protection of Patents in China*, in FOREIGN TRADE, INVESTMENT, AND THE LAW IN THE P.R.C. 471, n.3 (1987).

284. *Faming Jiangli Tiaoli* [Regulations of the People's Republic of China on Awards for Inventions], *promulgated* on Dec. 18, 1978, *amended* by the State Council on Apr. 25, 1984, *reprinted and translated* in 2 STATUTES AND REGULATIONS OF THE PEOPLE'S REPUBLIC OF CHINA, *supra* note 37, #840425.1 [hereinafter 1978 Invention Award Regulations].

285. *Id.*, art. 2.

no rights of ownership and protection in the invention, but is granted a considerable monetary reward.²⁸⁶ All Chinese inventors are to report their inventions to a series of bureaucratic organs "level by level in accordance with the related establishments."²⁸⁷ Foreign inventors and overseas Chinese residing abroad have the privilege of directly reporting to the State Commission of Science and Technology (SCST),²⁸⁸ which must approve the supply of certain classified contents of an invention under Article 10 to foreign trade or other causes.²⁸⁹

The 1984 Patent Law came into effect on April 1, 1985.²⁹⁰ It covers inventions, utility models, and designs.²⁹¹ In order to qualify for protection under the Patent Law, inventions or utility models must be novel, inventive, and practically applicable,²⁹² and designs must *not* be "identical . . . to any design which . . . has been publicly disclosed in publications" either in the P.R.C., or in other countries.²⁹³ Unpatentable items include "scientific disclosures, rules and methods for mental activities, methods for diagnosis or for the treatment of diseases, food, beverages and flavorings, pharmaceutical products and substances obtained by means of chemical process, animal and plant varieties, and substances obtained by means of nuclear transformation."²⁹⁴

The Chinese Patent Law follows the European "first to file" system rather than the U.S. "first to invent" system. Priority is given to the first inventor who applies for a patent. Priority is established on the date of the filed application.²⁹⁵ A foreign applicant who first files a patent application in a foreign country and thereafter files an application in the P.R.C. within a specified period of time for the same patent may enjoy a right of priority, in that the date on which the application was first filed in the said foreign country is regarded as the date of

286. *Id.*, arts. 8, 9. Article 8 guarantees a monetary award for an individual's invention. Article 9 provides that "[a]ll inventions belong to the state. Every unit in the whole country . . . can make use of the invention(s) when it needs to." According to the current Chinese standard, the amount of the award is considerable, ranging from ¥ 42,000 to ¥ 420,000 for each invention depending on the degree of its effect and significance. The grant of a "special-grade" award beyond the ¥ 420,000 limit is possible upon recommendation by the SCST and approval by the State Council. *Id.*, arts. 6, 7.

287. *Id.*, art. 5(1).

288. *Id.*, art. 12.

289. *Id.*, art. 11. For a brief history of China's patent system, see PENDLETON, *supra* note 252, at 18-19.

290. See People's Daily, Mar. 30, 1985, at 1.

291. 1984 Patent Law, *supra* note 278, art. 2.

292. *Id.*, art. 22.

293. *Id.*, art. 23.

294. *Id.*, art. 25.

295. *Id.*, art. 28.

filing in the P.R.C.²⁹⁶ The duration of protection under the patent laws varies with the type of creation seeking protection: the period of patent protection for inventions is fifteen (15) years, while the period of protection for utility models and designs is five (5) years, with the possibility of renewal for three additional years upon the patentee's application before the expiration date.²⁹⁷ Where the patentee enjoys a right of priority, the duration of protection under the patent laws begins from the date the application is filed in the P.R.C.²⁹⁸

To exploit the patented item in the best manner, the patentee is required to either manufacture the patented product, to use the patented process to manufacture the unpatented product, or to otherwise authorize its use.²⁹⁹ If the patentee fails to abide by this requirement within three (3) years without justification, a compulsory license will be granted by the Patent Office to allow others seeking a permit to export the patented item.³⁰⁰ The "licensee" who is granted a compulsory license must "contract" with the coerced "licensor" for reasonable royalties (the so-called "exploitation fee"). If the licensor and the licensee cannot reach an agreement on royalties, the Patent Office is authorized to adjudicate.³⁰¹

8.4. Other Industrial Property Rights

Audio-visual rights are also recognized and protected by Chinese law. The 1982 Interim Provisions on the Supervision of Sound and Video Recording Products³⁰² provide for royalty payments to the publishing unit which functions in a manner comparable to a copyright-collecting society.³⁰³ The 1985 Enterprise Names Regulations provide

296. *Id.*, art. 29. The specified time limit is twelve (12) months for patent applications for identical inventions or utility models and six (6) months for identical designs.

297. *Id.*, art. 45.

298. *Id.*

299. *Id.*, art. 51.

300. *Id.*, art. 52.

301. *Id.*, art. 57.

302. *Luyin Luxiang Zhipin Guanli Zanxing Guiding* [Interim Provisions on the Supervision of Sound and Video Recording Products], approved by the State Council, promulgated by the Ministry of Broadcasting and Television on Dec. 23, 1982, reprinted and translated in 1 STATUTES AND REGULATIONS OF THE PEOPLE'S REPUBLIC OF CHINA, *supra* note 37, at #821223 [hereinafter 1982 Interim Provisions].

303. Article 6 of the 1982 Interim Provisions reads as follows:

The publishing units of sound and video products shall safeguard the legitimate rights and interests of authors and performers. The standards for the remuneration of sound and video products of artistic items and the method of payment of the remuneration shall be jointly formulated by the Ministry of Broadcasting and Television and the Ministry of Culture.

The publishing units of sound and video products shall enjoy the

for registration of business names.³⁰⁴ The approved and registered name of an enterprise enjoys exclusive rights and legal protection within prescribed limits.³⁰⁵ The names of enterprises are assignable, provided that the assignor and the assignee sign a written assignment agreement and submit it to the industrial and commercial administration for examination and approval.³⁰⁶ Disputes arising from duplicative enterprise name use shall be settled in accordance with the order in which the enterprises' applications for registration were filed.³⁰⁷ Foreign enterprises are also required to register their business names with the SAIC.³⁰⁸

To the author's knowledge, the P.R.C. is currently studying the trade secret (confidential know-how) protection systems, unfair competition law, consumer protection law and licensing practices of other countries, and will be likely to promulgate special legislation regarding these matters in the future.³⁰⁹ The P.R.C.'s serious regard for international practice in this respect is illustrated by Article 7 of the 1985 Technology Import Contract Regulations, which obliges the recipient of foreign technology to "undertake the obligation to keep confidential . . . the technical secrets contained in the technology provided by the sup-

right to publish recorded sound and video data on the basis of their agreement with authors and performers. Any other unit shall not, without the authorization of an original publishing unit of a sound or video product, record or duplicate it, nor revise and imitate it for publication in another form. With regard to a programme which the author(s) and performer(s) have authorized a certain publishing unit of sound and video products to record and publish, another publishing unit of such products shall not record and publish it by means of increasing the remuneration or making another payment of remuneration or by other improper means. In case of violation, the original publishing unit of the sound or video product shall be entitled to lodge a complaint with the judicial authorities.

Id.

304. *Gong Shang Qiye Mingcheng Dengji Guanli Zanxing Guiding* [Provisional Regulations on the Registration of Names of Industrial and Commercial Enterprises], approved by the State Council on May 23, 1985, promulgated by the State Administration for Industry and Commerce on June 15, 1985, reprinted and translated in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 13-503 [hereinafter 1985 Enterprise Names Regulations].

305. *Id.*, art. 2.

306. *Id.*, art. 9.

307. *Id.*, arts. 7, 9.

308. *Id.*, art. 8.

309. *See NPC Faced with Heavy Legislative Tasks: Over 100 Enactments and Amendments in the Next Five Years*, People's Daily, Aug. 1, 1988, at 4. The NPC's legislation will focus on 55 laws being drafted which address the economic aspects. These include the drafting of the Law on the Prohibition of Unfair Competition, Law on the Protection of Consumer Rights and Interests, Law on Publications and Law on News Reporting.

plier, which have not been made public."³¹⁰

8.5. *Transfer of Technology*

8.5.1. *Applicable Laws*

The basic laws and regulations governing technology transfer include: 1) the 1985 Technology Import Contract Regulations;³¹¹ 2) the 1988 Technology Import Contract Rules;³¹² 3) 1985 Technology Transfer Regulations;³¹³ 4) 1987 Technology Contract Law;³¹⁴ and 5) various provisions in the Joint Venture Law, the Joint Venture Law Implementation Regulations, the Co-Operative Enterprise Law and the Wholly Foreign-Owned Enterprise Law.³¹⁵ Also, it is expected that the P.R.C. will enact a Technology Import Law in 1989.³¹⁶

8.5.2. *General Provisions and Practice*

8.5.2.1. *Technology Import.* The 1985 Technology Import Contract Regulations and the 1988 Technology Import Contract Rules regulate the import and transfer of patents, technological processes, prescriptions, products, designs, technical services, and any combination of these.³¹⁷

310. *Jishu Yinjin Hetong Guanli Tiaoli* [Regulations on Administration of Technology Import Contracts of the People's Republic of China], art. 7, *promulgated* by the State Council on May 24, 1985, *reprinted and translated* in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 5-570 [hereinafter 1985 Technology Import Contract Regulations].

311. *Id.*

312. *Jishu Yinjin Hetong Guanli Tiaoli Shixing Xize* [Detailed Rules for Implementation of the Regulations on Administration of Technology Import Contracts of the People's Republic of China], *approved* by the State Council on Dec. 30, 1987, *promulgated* by MOFERT on Jan. 20, 1988, art. 7, *reprinted and translated* in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 5-593 [hereinafter 1988 Technology Import Contract Rules].

313. *Guanyu Jishu Zhuanrang de Zanxing Guiding* [Provisional Regulations of the State Council on Technology Transfer], *promulgated* by the State Council on Jan. 10, 1985, *reprinted and translated* in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 19-536 [hereinafter 1985 Technology Transfer Regulations].

314. *Jishu Hetong Fa* [Law of the People's Republic of China on Technology Contracts], *adopted* by the Twenty-First Session of the Standing Committee of the Sixth National People's Congress on June 23, 1987, *reprinted and translated* in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 5-577 [hereinafter 1987 Technology Contract Law].

315. Joint Venture Law, *supra* note 36, at ¶ 6-500, arts. 5, 7, 9; Joint Venture Implementation Regulations, *supra* note 52, at ¶ 6-550, arts. 3, 11; Wholly Foreign-Owned Enterprise Law, *supra* note 37, at ¶ 13-506.

316. *See News Reports on the Promulgation of the 1988 Technology Import Contract Rules*, People's Daily, Jan. 21, 1988, at 1.

317. 1985 Technology Import Contract Regulations, *supra* note 311, art. 2. Technology imports include the "[a]ssignment or licensing of patents or other industrial

The import and export of technology, especially "pure" technology licensing or assignment arrangements, are usually handled through FTCs empowered to do so. Important FTCs in technology transfer include CITIC, TECHIMPEX (China National Technical Import & Export Corporation), and a new establishment under the CCPIT specializing in patent and other technology licensing and assignment.³¹⁸

The 1988 Rules clarify the scope of the 1985 Regulations. Under the Rules, the following types of contracts shall be covered by the 1985 Technology Import Contract Regulations: 1) "industrial property rights" assignment or licensing contracts; 2) technological know-how licensing contracts; 3) technical service contracts; 4) co-operative production contracts or co-operative designing contracts involving assignment or licensing of industrial property rights, licensing of know-how, or technical services; 5) equipment importing contracts involving assignment or licensing of industrial property rights, licensing of know-how, or technical services; and 6) other technology import contracts.³¹⁹ The Chinese technology importer is required to maintain the confidentiality of imported technology or know-how, but this obligation usually does not exceed the duration of the contract unless, subject to approval by the MOFERT, the technology importing contract explicitly provides terms to the contrary.³²⁰ The above Regulations and Rules extend their application to technology import contracts concluded between P.R.C.-based foreign investment enterprises (i.e., the so-called *san-zi qiye* — joint ventures, co-operative enterprises, and wholly foreign-owned enterprises) as the importer of technology and foreign technology suppliers as exporters. These provisions however, do not apply to cases where the foreign investors of *san-zi qiye* provide industrial property rights or trade secrets as their investment to their projects in the P.R.C. Under such circumstances, the relevant laws and regulations concerning foreign investment enterprises are applicable.³²¹

8.5.2.2. Quality Requirement. Technology or equipment imported by joint ventures must be truly advanced and suited to the P.R.C.'s needs.

property rights. . . [k]now-how provided in the form of drawings, technical data, technical specifications, etc., such as production processes, formulas, production designs, quality control and management skills," and "[t]echnical services." *Id.*

318. See *China Patent and Technology Transfer Co., Ltd. Opens Its Business*, People's Daily, Nov. 25, 1987, at 8.

319. 1988 Technology Import Contract Rules, *supra* note 312, art. 2. It is interesting to note that the Rules do not treat trade secrets (know-how) as an industrial property right.

320. *Id.*, art. 13. See also, 1985 Technology Import Contract Regulations, *supra* note 310, art. 7.

321. 1988 Technology Import Contract Rules, *supra* note 312, art. 4.

In order to encourage the import of advanced technology, the Joint Venture Law provides that a joint venture equipped with technology considered advanced by international standards may apply for a reduction of or exemption from income tax for its first three (3) profit-making years. Should obsolete or dated technology be imported through deceptive practices, the importer would be required to pay compensation for losses incurred as a result of the intentional use of the backward technology or equipment.³²² The laws on the other two forms of foreign investment enterprises are softer in this regard. A wholly foreign-owned enterprise is required either to adopt advanced technology and equipment *or* export all or most of its products.³²³ No such requirement even exists for a contractual joint venture. The state merely *encourages* the establishment of productive co-operative enterprises that are technologically advanced or are export-oriented.³²⁴

8.5.2.3. Technology Transfers. In recognizing that technology is a commodity which is transferable, the State Council promulgated the 1985 Technology Transfer Regulations after deciding to open the technology market and to promote technology trade. Under this promulgation, "units and individuals may all transfer technology free of the restrictions of regional, departmental or economic structure," and "the transferor and transferee may engage in technology transfer in accordance with the principles of voluntary participation and mutual benefit and agreement through consultation."³²⁵ The transfer fee refers to the "price for an item of technology, following adjustment in the market and consultation and agreement between the two parties."³²⁶ Payment can be either in a lump sum, a fixed percentage of increased sales or profits deriving from the implementation of the transferred technology, or any other method agreed upon between the transferor and the transferee.³²⁷ A technology transfer agreement must conform to the Economic Contract Law and the relevant provisions of other laws.³²⁸ Other coverage includes rights and interests in technology transfer,³²⁹ pay-

322. Joint Venture Law, *supra* note 36, arts. 5, 7. See 1982 Offshore Petroleum Regulations, *supra* note 106, art. 12 (foreign contractor "shall use appropriate and advanced technology and management experience and shall be obliged to transfer the technology and pass on the experience to the personnel of the Chinese side," and shall employ a certain percentage of Chinese staff and workers and provide training to them in a planned way).

323. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 3.

324. Co-Operative Enterprise Law, *supra* note 38, art. 4.

325. 1985 Technology Transfer Regulations, *supra* note 313, art. 1.

326. *Id.*, art. 3.

327. *Id.*

328. *Id.*, art. 2.

329. *Id.*, art. 4.

ment of technology transfer fees,³³⁰ taxation of technology transfer,³³¹ and use of the income from technology transfers.³³²

8.5.2.4. Technology Contracts. The 1987 Technology Contract Law came into force on November 1, 1987.³³³ Its purpose is to further the P.R.C.'s scientific and technological development, to promote the use of science and technology as a means to further the P.R.C.'s modernization, to protect the legitimate rights and interests of parties to technology contracts, and to maintain "good order" in the technology market.³³⁴ In its 55 articles and 7 chapters, the following major legal aspects of technology contracts are dealt with: 1) formation, performance, modification, and termination of technology contracts;³³⁵ 2) technical development contracts;³³⁶ 3) technology transfer contracts;³³⁷ 4) technical consultancy contracts and technical service contracts;³³⁸ and 5) arbitration and litigation of technology contract disputes.³³⁹

The Technology Contract Law applies only to Chinese citizens and legal persons, but not to "contracts in which one party is a foreign enterprise, other foreign organization or foreign individual."³⁴⁰ It is not clear whether a contract to which a Chinese-foreign joint venture is a party is subject to this legislation. The situation is also ambiguous for a wholly foreign-owned enterprise which is both a duly approved, registered and licensed Chinese legal person on the one hand, and a completely *foreign*-owned entity on the other. A news report by the Xinhua (New China) News Agency seems to have resolved this problem: *san zi qiye* (Sino-foreign equity joint ventures, Sino-foreign co-operative business enterprises, and wholly foreign-owned enterprises) "operating within the Chinese territory" are all deemed Chinese legal persons, and the Technology Contract Law applies equally to technology contracts made between *san zi qiye* and Chinese citizens or other Chinese legal entities.³⁴¹

330. *Id.*, art. 5.

331. *Id.*, art. 6.

332. *Id.*, art. 7.

333. *The Technology Contract Law Coming Into Implementation Today*, People's Daily, Nov. 1, 1987, at 1.

334. 1987 Technology Contract Law, *supra* note 314, art. 1.

335. *Id.* ch. II.

336. *Id.* ch. III.

337. *Id.* ch. IV.

338. *Id.* ch. V.

339. *Id.* ch. VI.

340. *Id.* art. 2.

341. *The Technology Contract Law Coming into Implementation Today*, *supra* note 333.

9. TAXATION

For the purposes of this article, it is sufficient to survey briefly the basic aspects of the P.R.C.'s taxation system as it affects foreign investment.³⁴² The development of tax legislation relating to foreign investment in the P.R.C. is not well-balanced. Even in the area of equity joint ventures where tax regulations are the most complete, it is still very ambiguous and difficult to judge the merits, demerits, applicability, and development of the tax laws because many of the joint ventures established are not yet in full operation, and others are still enjoying tax holidays.

Generally speaking, foreign-invested enterprises in the P.R.C. are subject to five types of taxation: 1) consolidated industrial and commercial tax; 2) enterprise income tax; 3) individual income tax; 4) urban building and land taxes; and 5) vehicles and ships license dues.³⁴³ Before discussing the five tax areas, it is necessary to note some problems. First, although specific legislation has been in existence, it is difficult to advise others with any degree of certainty. For example, there are often different practices from tax bureau to tax bureau, within the same tax bureau, or even by the same tax official, in applying the same tax rule to different taxpayers.³⁴⁴ However, serious problems concerning the payment of income taxes by foreign investment enterprises and their employees has not appeared because specific legislation has been recently enacted in this regard.³⁴⁵

342. For articles on this subject, see generally Castleman, *Taxation in the People's Republic of China: The System and Its Function*, 46 ALB. L. REV. 777 (1982); Clarke, *Taxation of Joint Ventures, Foreign Enterprises, and Individuals in the PRC*, in LEGAL ASPECTS OF DOING BUSINESS WITH THE PEOPLE'S REPUBLIC OF CHINA 289-303 (1986); Pomp, Gelatt, & Surrey, *The Evolving Tax System of the People's Republic of China*, 16 TEX. INT'L L.J. 11 (1981); Pomp, & Surrey, *The Tax Structure of the People's Republic of China*, 20 VA. J. INT'L L. 1 (1979); Reynolds, *Doing Business with the People's Republic of China: Tax Considerations*, 14 INT'L LAW. 49 (1980); Note, *The Joint Ventures Law of the People's Republic of China in a Legislated and Negotiated Tax Climate*, 8 SYRACUSE J. INT'L L. & COM. 227 (1980); Note, *Taxation of Joint Ventures in the People's Republic of China*, 15 VAND. J. TRANSNAT'L L. 513 (1982).

343. *What Taxes to Pay by Foreigners Investing in China?*, People's Daily, Sept. 23, 1987, at 3.

344. See Clarke, *supra* note 342, at 291.

345. See, e.g., Joint Venture Income Tax Law, *supra* note 45; Joint Venture Income Tax Rules, *supra* note 83; Foreign Enterprise Income Tax Law, *supra* note 46; *Waiguo Qiye Suode Shui Fa Shixing Xizao* [Detailed Rules and Regulations for the Implementation of the Foreign Enterprise Income Tax Law of the People's Republic of China], approved by the State Council on Feb. 17, 1982, promulgated by the Ministry of Finance on Feb. 21, 1982, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18 at ¶ 32-510 [hereinafter Foreign Enterprise Income Tax Rules]; *Geren Suode Shui Fa* [Individual Income Tax Law of the People's Republic of China], adopted and promulgated by the Third Session of the Fifth National People's Con-

Second, many tax rules are "old" rules, and even some newly enacted tax laws are subject to revision. One can often read from newspapers and other sources statements and speeches made by Chinese leaders and high level officials indicating that in order to create a more attractive investment environment, necessary changes in tax rules and other regulations will be made from time to time. In addition, the P.R.C. has been making efforts to adopt international practices in tax matters.³⁴⁶ This innocent trend has caused concern amongst foreign investors and legal experts as it has been criticized for possibly "result[ing] in taxing previously exempt income."³⁴⁷ This concern is an unnecessary one. Even if the trend would actually affect the tax exemptions currently enjoyed by foreign investors (especially foreign joint venturers), the overall benefits would be more substantial to foreign investors as a result of the adoption of international practices. Moreover, no matter what usage or practice will be adopted, the P.R.C. will only increase the environment's attractiveness to foreign investors without losing its long-term benefits. Third, it is important, to determine whether there is a tax treaty or agreement in force between the P.R.C. and the foreign country concerned. As of December 1987, the People's Republic of China maintained tax agreements with 18 countries which include the following countries: Belgium, Canada, Denmark, Finland, the Federal Republic of Germany, France, Italy, Japan, Malaysia, New Zealand, Norway, Thailand, the United Kingdom, and the United States.³⁴⁸

9.1. Consolidated Industrial and Commercial Taxes

9.1.1. The Applicable Laws

A number of laws and regulations comprise what is known as the Consolidated Industrial and Commercial Tax. Since they were enacted in the 1950's, many of these laws and regulations are in need of revision or re-enactment. They are still in force, however, and are applicable to foreign investment enterprises. Enactments affecting foreign in-

gress on Sept. 10, 1980, *reprinted and translated in id.* at ¶ 30-500 [hereinafter Individual Income Tax Law]; *Geren Suode Shui Fa Shixing Xize* [Detailed Rules and Regulations for the Implementation of the Individual Income Tax Law of the People's Republic of China] *approved by the State Council on Dec. 10, 1980, promulgated by the Ministry of Finance on Dec. 14, 1980, reprinted and translated in id.* at ¶ 30-520 [hereinafter Individual Income Tax Rules].

346. Clarke, *supra* note 342, at 291.

347. *Id.*

348. See *China Enacted Over 200 Pieces of Foreign Economic Laws and Regulations*, *People's Daily*, Dec. 19, 1987, at 1, col. 1.
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vestment enterprises include: 1) the 1958 Consolidated Industrial and Commercial Tax Regulations;³⁴⁹ 2) the 1958 Consolidated Industrial and Commercial Tax Detailed Rules;³⁵⁰ 3) the 1982 Tax Rate Adjustments Notifications;³⁵¹ 4) the 1984 Value Added Tax Regulations;³⁵² 5) the 1984 Product Tax Regulations;³⁵³ 6) the 1985 Foreign Resident Representative Office Tax Collection Provisions;³⁵⁴ and 7) the 1986 Notice on Refrigerators and Other Products.³⁵⁵

9.1.2. Scope and Method

The 1958 Consolidated Industrial and Commercial Tax Regulations have been modified and are still in force. The Regulations combine and simplify aspects of the former Commodity Tax, Commodity Circulation Tax, Business Tax and the Revenue Stamp Tax.³⁵⁶ They

349. *Gong Shang Tongyi Shui Tiaoli (Cao'an)* [The Regulations of the Consolidated Industrial and Commercial Tax of the People's Republic of China (Draft)], adopted by the One Hundred and First Meeting of the Standing Committee of the National People's Congress on Sept. 11, 1958, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 31-500 [hereinafter Consolidated Tax Regulations].

350. *Gong Shang Tongyi Shui Tiaoli Shixing Xize Cao'an* [Detailed Rules and Regulations for the Implementation of the Regulations of the Consolidated Industrial and Commercial Tax of the People's Republic of China (Draft)], promulgated by the Ministry of Finance on Sept. 13, 1958, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 31-510 [hereinafter Consolidated Tax Rules].

351. *Guanyu Tiaozheng Gong Shang Shui Ruogan Chanpin Shuilü he Kuoda Zhengshui Xiangmu De Tongzhi* [Finance Ministry's Notification Concerning the Adjustment of Commercial and Industrial Tax Rates on Certain Categories of Products and the Extension of Taxable Items], promulgated on June 10, 1982, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 31-560 [hereinafter 1982 Tax Rate Adjustment Notification].

352. *Zeng Zhi Shui Tiaoli (Cao'an)* [Regulations of the People's Republic of China on Value Added Tax (Draft)], promulgated by the State Council on Sept. 18, 1984, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 31-700 [hereinafter 1984 Value Added Tax Regulations].

353. *Chanpin Shui Tiaoli (Cao'an)* [Regulations of the People's Republic of China on Product Tax (Draft)], promulgated by the State Council on Sept. 18, 1984, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 31-708 [hereinafter 1984 Product Tax Regulations].

354. *Dui Waiguo Qiye Changzhu Daibiao Jigou Zhengshou Gong Shang Tongyi Shui, Qiye Suode Shui de Zanxing Guiding* [Provisional Regulations for Collection of Consolidated Industrial and Commercial Tax and Enterprise Income Tax from Resident Representative Offices of Foreign Enterprises], issued by the Ministry of Finance on May 15, 1985, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 31-600 [hereinafter 1985 Foreign Resident Representative Office Tax Collection Provisions].

355. *Guanyu Dianbingxiang Deng Chanpin Shiyong Gong Shang Tongyi Shui Shuilü De Tongzhi* [Notice of the Ministry of Finance Concerning Applicable Rates of Consolidated Industrial and Commercial Tax on Refrigerators and Other Products], promulgated on Apr. 18, 1986, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 31-605 [hereinafter 1986 Notice on Refrigerators and Other Products].

356. See Consolidated Tax Regulations, *supra* note 349, art. 1.
<https://scholarship.law.upenn.edu/jil/vol10/iss3/4>

are composed of 19 articles including a tax schedule, and are supplemented by the 35 articles of the Detailed Rules for Implementation.³⁵⁷ All "units or individuals" within the P.R.C. which are engaged in the production of industrial products, the purchase of agricultural products, the importation of foreign goods, commercial retailing, communications and transportation, and all other service trades are subject to the Consolidated Tax Regulations.³⁵⁸ Foreign firms and individuals doing business in the P.R.C. are clearly covered under this provision. Those specifically engaged in industrial production are taxed on the sale of the industrial products which are produced. The tax is calculated at specified rates which are based on the proceeds received from the sale.³⁵⁹ Those purchasing agricultural products, compute the tax on the basis of the amount paid for the purchase.³⁶⁰ Those importing foreign goods, after the importation, pay a tax which is based on the amount paid for the import.³⁶¹ Those engaged in commercial retailing pay a tax based on the proceeds received from the retail sale.³⁶² Finally, those engaged in communications and transportation as well as all other service trades pay a tax based on the amount of proceeds received from the business.³⁶³ Thus, the Consolidated Tax is levied at every level of production and retail where goods are transferred from one level to another. When goods are sold to the end-user, no credit is given for any tax which has already been paid by others on the same item. No exemption exists for further resales.³⁶⁴

9.1.3. *Taxable Items and Tax Rates*

The Consolidated Tax rates for each item taxable thereunder are specified in the annexed tax schedule of the Consolidated Tax Regulations, which includes over 40 different rates applicable to more than 100 items ranging from 1.5% for grey cotton goods to 69% for high-quality cigarettes. The rates for most taxable industrial products, on the other hand, range from 5% to 15%.³⁶⁵ Furthermore, Article 3 of the Regulations allow the addition, deletion, or adjustment of the items to be taxed as well as the rates to be determined and promulgated by the

357. See Consolidated Tax Rules, *supra* note 350.

358. Consolidated Tax Regulations, *supra* note 349, art. 2.

359. *Id.*, art. 4.

360. *Id.*, art. 5.

361. *Id.*, art. 6.

362. *Id.*, art. 7.

363. *Id.*, art. 8.

364. See Lussenburg, *supra* note 101, at 577.

365. Taxable Items and Rates of the Consolidated Industrial and Commercial

Tax in Consolidated Tax Regulations, *supra* note 349.

State Council.³⁶⁶

9.1.4. Exemptions

Recent enactments concerning foreign investment have added exemptions to the Consolidated Tax. For instance, under the Joint Venture Law Implementation Regulations, imports of machinery, equipment, spare parts, and other items which comprise the primary contribution of the foreign partner of the joint venture contract are exempt from custom duties and consolidated industrial and commercial tax.³⁶⁷ Also included are instances in which goods are imported with capital which is also part of the joint venture's total investment, and instances in which goods for which the P.R.C. cannot guarantee production or supply are imported with extra capital, subject to approval by the examining and approving body as a security measure.³⁶⁸ Similarly, raw materials, auxiliary materials, components, spare parts, and packaging materials imported by a joint venture for the production of export goods³⁶⁹ are also exempt from these duties and taxes.³⁷⁰ However, where the joint venture resells the duty-free imported materials within the P.R.C., or where its goal becomes the sale of its products manufactured with the use of the imported items, it must then pay back the appropriate customs duties and consolidated tax.³⁷¹

There are currently no formal regulations or practices exempting contractual joint ventures and wholly foreign-owned enterprises from the consolidated industrial and commercial tax.

9.2. Enterprise Income Tax

9.2.1. The Applicable Laws

Legislation and regulations on income taxes have been promulgated for foreign investment enterprises. The list of governing laws here is even longer than that relating to the consolidated tax. There is,

366. *Id.*, art. 3.

367. Joint Venture Law Implementation Regulations, *supra* note 52, art. 71.

368. *Id.*

369. A joint venture's export products may be exempt from the consolidated industrial and commercial tax subject to the State's export provisions and upon approval by the Ministry of Finance. In the event that the joint venture has difficulty paying its consolidated tax for domestic sales of its products during the initial period of operation, it may apply for a reduction or exemption of the tax for a limited period of time. *See id.*, art. 72.

370. *Id.*, art. 71(4).

371. *Id.*, art. 71.

for example, the 1981 Foreign Enterprise Income Tax Law³⁷² and the 1982 Foreign Enterprise Income Tax Rules³⁷³ which regulate the income tax matters of all foreign investment enterprises, with the exception of equity Sino-foreign joint ventures. There is also the 1980 Joint Venture Income Tax Law³⁷⁴ and the 1980 Joint Venture Income Tax Rules³⁷⁵ which exclusively deal with Sino-foreign equity joint ventures. Finally, there is the 1983 Interest Tax Reduction and Exemption Regulations,³⁷⁶ the 1987 Preferential Tax Treatment Measures³⁷⁷ and the 1986 Income Tax Levying Notice,³⁷⁸ which are all common provisions on foreign-invested enterprise income tax matters.

9.2.2. *Joint Venture Income Tax*

As mentioned earlier, perhaps the most obvious advantage of joint ventures are the tax advantages. For instance, the exemptions from custom duties and consolidated industrial and commercial tax are broader, the income tax rate lower and the tax holidays more generous, unlike joint ventures, which are governed by separate income tax laws and regulations. This is indicative of the State's preference for and special treatment of equity joint ventures.

9.2.2.1. *Scope.* The income tax is levied on a joint venture's income from production, business, and other sources. Its branches' income tax on the income derived from the same sources is to be collectively paid by the head office, regardless of whether such branches are in the

372. Foreign Enterprise Income Tax Law, *supra* note 46.

373. Foreign Enterprise Income Tax Rules, *supra* note 345.

374. Joint Venture Income Tax Law, *supra* note 45.

375. Joint Venture Income Tax Rules, *supra* note 83.

376. *Guanyu Wai Shang Cong Woguo Suode De Lixi Youguan Jianmian Suode Shui De Zanxing Guiding* [Provisional Regulations of the Ministry of Finance of the People's Republic of China Regarding the Reduction and Exemption of Income Tax Relating to Interest Earned by Foreign Businesses from China], promulgated by the Ministry of Finance on Jan. 1, 1983, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 32-600 [hereinafter 1983 Interest Tax Reduction and Exemption Regulations].

377. Measures of the Ministry of Finance for the Implementation of the Preferential Tax Treatment Provisions of the State Council Regulations Concerning Encouragement of Foreign Investment, issued by the Ministry of Finance on Jan. 31, 1987, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 32-650 [hereinafter 1987 Preferential Tax Treatment Measures].

378. Notice of the General Taxation Bureau of the Ministry of Finance Concerning Several Regulations Relating to the Levying of Income Tax on Sino-Foreign Joint Equity Enterprises and Co-operative Production Enterprises, and Enterprises with Sole Foreign Investment of Apr. 21, 1986, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 33-515 [hereinafter 1986 Income Tax Levying Notice].

P.R.C. or abroad.³⁷⁹

9.2.2.2. Taxable Income. The taxable income of a joint venture is the net income after deducting the costs, expenses and losses in a single tax year.³⁸⁰ The net income includes income derived from production, business operations and other sources such as bonuses, interest, royalties, and rental income.

9.2.2.3. Tax Rates. The income tax rate for joint ventures is 30% in addition to a local surtax of 10% on the amount of the assessed income tax.³⁸¹ In addition, a separate withholding tax of 10% is charged in the event the foreign partner of a joint venture remits its share of profits out of the P.R.C.³⁸² In this situation, the combined income tax rate for the foreign party would be 39.7%. Foreign partners who intend to remit their share of profits from the P.R.C. are responsible for informing the local tax authorities so that the 10% tax will be withheld by the remitting agency.³⁸³

9.2.2.4. Tax Incentives and Holidays.

(a) The tax incentives and tax holidays³⁸⁴ for joint ventures are significant. Amended Article 5 of the Joint Venture Income Tax Law provides that "[a] joint venture scheduled to operate for a period of 10 years or more may, upon approval by the tax authorities of an application filed by the enterprise, be exempted from income tax in the first and second profit-making years and allowed a 50% reduction in the third to fifth years."³⁸⁵ In other words, when a joint venture begins to become profitable the foreign partner would pay no income tax for the first two profitable years and would thereafter pay only 16.5% of its net income in the next three profitable years (or 19.85% if it chooses to remit its shares of profits out of the P.R.C.).

(b) Reinvestment in the P.R.C. for five consecutive years entitles a joint venture to a 40% refund on income taxes paid on reinvested funds.³⁸⁶

(c) In any tax year, losses incurred by a joint venture may be carried over to the next tax year and matched with an identical amount

379. Joint Venture Income Tax Law, *supra* note 45, art. 1.

380. *Id.*, art. 2.

381. *Id.*, art. 3.

382. *Id.*, art. 4.

383. Joint Venture Income Tax Rules, *supra* note 83, art. 5.

384. A tax holiday is the period of time during which the ventures enjoy tax exemptions.

385. Joint Venture Income Tax Law, *supra* note 45, art. 5.

386. *Id.*, art. 6.

drawn from that year's income. Further deductions against income are allowed on a year-to-year basis. Carryovers for any particular joint venture may not exceed five years.³⁸⁷

(d) Joint ventures engaged in low-profit operations such as farming, forestry or operations located in remote, economically underdeveloped outlying areas may be permitted a 15-30% reduction in income tax for 10 years following the expiration of the initial five-year tax holiday.³⁸⁸

(e) Taxes paid abroad by a joint venture or its branches on their foreign-earned income may be credited against the income tax to be paid by its head office in the P.R.C. However, such credit may not exceed the Chinese tax payable on the income received abroad.³⁸⁹

9.2.3. *Foreign Enterprise Income Tax*

Foreign investment enterprises other than equity joint ventures are governed by the 1981 Foreign Enterprise Income Tax Law³⁹⁰ and the 1982 Foreign Enterprise Income Tax Rules.³⁹¹

9.2.3.1. *Scope.* Foreign enterprises operating in the P.R.C. are defined in article 1 of the Foreign Enterprise Income Tax Law as "foreign companies, enterprises and other economic organizations which have establishments in the P.R.C. engaged in independent business operation or co-operative production or joint business operation with Chinese enterprises."³⁹² Such enterprises are all subject to the income tax that is to be levied in accordance with the said Law on the income derived from their production, business, and other sources. However, foreign companies, enterprises and other economic organizations having no establishments in the P.R.C., but which derive certain types of "passive income" from Chinese sources, such as dividends, interest, rentals, and royalties, are subject to a withholding tax.³⁹³ Chinese and foreign enterprises which are engaged in co-operative production or joint business operations pay their own income taxes respectively, unless their

387. *Id.*, art. 7.

388. *Id.*, art. 5.

389. *Id.*, art. 16. *See also*, Joint Venture Income Tax Rules, *supra* note 83, art. 32.

390. Foreign Enterprise Income Tax Law, *supra* note 46.

391. Foreign Enterprise Income Tax Rules, *supra* note 345.

392. Foreign Enterprise Income Tax Law, *supra* note 46, art. 1.

393. *Id.*, art. 11.

contract provides otherwise.³⁹⁴

9.2.3.2. Taxable Income. The taxable income of a foreign enterprise operating in the P.R.C. is the net income derived from production, business and other sources (including dividends, interest, income from the lease or sale of property, income from the transfer of patents, technical know-how, trademark interests or copyright, and other non-business income) in a tax year after the deduction of costs, expenditures, and losses in the said year.³⁹⁵ The taxable income of foreign enterprises having no establishments in the P.R.C. within the meaning of article 11 of the 1981 Foreign Enterprise Income Tax Law is to be assessed on the gross amount (full amount) of such income from Chinese sources, and the tax is to be withheld by the paying unit from each payment.³⁹⁶

9.2.3.3. Tax Rates. The income tax rates for foreign enterprises having establishments in the P.R.C. ranges from 20% to 40% depending upon the income in a tax year. The tax rate for annual income up to ¥ 250,000³⁹⁷ is 20%; for annual income between ¥ 250,000 and ¥ 450,000, the rate is 25%; for annual income between ¥ 500,000 and ¥ 750,000, the rate is 30%; for annual income between ¥ 750,000 and ¥ 1,000,000, the rate is 35%; and for annual income exceeding ¥ 1,000,000 the tax rate is 40%.³⁹⁸ In addition, a local income-tax of 10% is levied on the same taxable income.³⁹⁹ Lastly, the income tax rate for income derived from Chinese sources by foreign enterprises without establishments in the P.R.C. is 20%.⁴⁰⁰

9.2.3.4. Tax Incentives.

(a) Foreign enterprises engaged in farming, forestry, animal hus-

394. Foreign Enterprise Income Tax Rules, *supra* note 345, art. 3.

395. Foreign Enterprise Income Tax Law, *supra* note 46 arts. 1, 2; Foreign Enterprise Income Tax Rules, *supra* note 345, art. 4.

396. Foreign Enterprise Income Tax Rules, *supra* note 345, art. 28.

397. "¥" is the symbol of the Chinese RMB uan. Under the current official exchange rate, US \$100 = RMB ¥ 372.

398. Foreign Enterprise Income Tax Law, *supra* note 46, art. 3.

399. *Id.*, art. 4. Note that the local income tax in this instance is not a surtax on the income tax, as is the case with joint ventures.

400. *Id.*, art. 11. The "foreign companies, enterprises . . . establishments in China" provision does not include foreign companies operating in the SEZs. According to the Foreign Enterprise Income Tax Rules, the word "establishments" refers to "organizations, places or business agents established in Chinese territory by foreign enterprises engaged in production and business operations." They "mainly include management offices, branches, representative offices, factories and places where natural resources are exploited and where contracted projects of building, installations, assembly and exploration are operated." Foreign Enterprise Income Tax Rules, *supra* note

bandry or other low-profit occupations and which are scheduled to operate for 10 or more years may, subject to approval by the tax authorities, be exempt from income tax in the first profit-making year and allowed a 50% reduction in the second and third profit-making years. Upon the expiration of these tax holidays, a further 15-30% reduction in income tax may be permitted for a ten-year period if a request is made and approved by the Ministry of Finance.⁴⁰¹

(b) If a foreign enterprise needs a reduction in, or an exemption from local income tax "on account of the small-scale of its production or business, or its low rate of profit," it may request it from the local People's Government.⁴⁰² The decision to grant a reduction or an exemption is left to the local Government's discretion. However, most local Governments give due consideration to all requests.

(c) If losses are incurred by a foreign enterprise in a tax year, they may be carried over and deducted from taxable income in the following year. If income in the following tax year is insufficient to cover previous losses, the balance may then be deducted from taxable income in future years for a five year period.⁴⁰³

9.3. Individual Income Tax

9.3.1. The Applicable Laws

The 1980 Individual Income Tax Law⁴⁰⁴ and the 1980 Individual Income Tax Rules⁴⁰⁵ apply equally to foreign nationals and to Chinese employees who work in a foreign investment enterprise as well as to ordinary Chinese citizens. Both laws are, in fact, primarily directed to individuals who are employed in foreign investment enterprises and other foreign-related services because few Chinese citizens in the regular professions earn enough to be taxed under the 1980 Individual Income Tax Law. Also relevant are the 1987 Foreign Nationals Income Tax Reduction Provisions, which are explicitly concerned with foreigners.⁴⁰⁶

345, art. 2.

401. Foreign Enterprise Income Tax Law, *supra* note 46, art. 5.

402. *Id.*, art. 4.

403. *Id.*, art. 6.

404. Individual Income Tax Law, *supra* note 345.

405. Individual Income Tax Rules, *supra* note 345.

406. *Guowu Yuan Guanyu Dui Lai Hua Gongzuo De Waiji Renyuan Gongzi, Xinjin Suode Jianzheng Suode Shui De Zanxing Guiding* [Provisional Regulations of the State Council Concerning the Reduction of Individual Income Tax on Wages and Salaries of Foreign Nationals Working in China], promulgated by the State Council on Aug. 8, 1987, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 30-528 [hereinafter, 1987 Foreign Nationals Income Tax Reduction Provisions].

9.3.2. *Scope*

Individuals who have resided for more than one year in the P.R.C. and who receive income from sources either within or without the P.R.C. are subject to Chinese individual income tax provisions. For individuals who do not reside in the P.R.C. or who have resided in the P.R.C. for less than one year, individual income tax will only be levied on income gained from sources within the P.R.C.⁴⁰⁷

9.3.3. *Taxable Income*

The taxable individual income includes: 1) wages and salaries; 2) compensation for personal services; 3) royalties; 4) interest, dividends and bonuses; 5) income from leasing property; and 6) other incomes determined to be taxable by the Ministry of Finance.⁴⁰⁸

9.3.4. *Tax Rates*

The tax rates for income from wages and salaries are progressive and range from 5% to 45%.⁴⁰⁹ Individual income from wages and salaries not exceeding ¥ 800 per month is exempt from tax and the rate of tax for individual income received as compensation for personal services, royalties, interest, dividends, bonuses and other sources is a flat 20%.⁴¹⁰

407. Individual Income Tax Law, *supra* note 345, art. 1.

408. *Id.*, art. 2. Under the Individual Income Tax Rules, "wages and salaries" include wages, salaries, money awards, and year-end salary raises gained by individuals from work in offices, organizations, schools, enterprises, undertakings and other entities, but prizes and awards for scientific, technological, or cultural achievements are not included. "Income derived from compensation for personal services" is defined as income gained by individuals from engaging in services such as designing, installation, lecturing, news, broadcasting, contributions to publications, translation, calligraphy, painting, sculpture, movies, music, drama, dancing, acrobatics, singing, sports, technical services, and the like. *Id.*, art. 4(2). "Royalties" include income from the provision or assignment of patent rights, copyrights and the right to use proprietary technology. *Id.*, art. 4(3). "Interest, dividends and bonuses" mean interest on deposits, loans and bonds and dividends and bonuses from investments. *Id.*, art. 4(4).

409. *Id.*, art. 3. For monthly income ranging from ¥ 801 to ¥ 500, the tax rate is 5%; for monthly income ranging from ¥ 501 to ¥ 3,000, the tax rate is 10%; for monthly income ranging from ¥ 3,000 to ¥ 6,000, the tax rate is 20%; for monthly income ranging from ¥ 6,000 to ¥ 9,000, the tax rate is 30%; for monthly income ranging from ¥ 9,000 to ¥ 12,000, the tax rate is 40%; and for monthly income exceeding ¥ 12,000 the tax rate is 45%. See *id.*, the Appended Individual Income Tax Rate Table.

410. *Id.*, art. 3(2).

9.3.5. *Tax Reductions and Exemptions*

Foreign nationals who 1) work for a Chinese-foreign equity joint venture, Chinese-foreign co-operative enterprise or wholly foreign-owned enterprise operating in the P.R.C., or 2) work in the P.R.C.-based representative office of a foreign company, enterprise or other economic organizations, or 3) otherwise work in the P.R.C., have the privilege of paying only one-half the amount of individual income tax payable on their wages under the 1980 Individual Income Tax Law.⁴¹¹ The income tax payable on the wages or salaries of an overseas Chinese, Hong Kong or Macao compatriot working in the P.R.C. is similarly reduced.⁴¹² The provisions are broad enough to include, for example, foreign teachers and experts working in Chinese educational institutions. These new provisions render the corresponding stipulations in the 1980 Individual Income Tax Law almost meaningless, because very few Chinese earn more than the minimum taxable income of ¥ 800 per month.

Exemptions from individual income tax are allowed for certain types of income, including awards for scientific, technological or cultural achievements, interest on savings deposited in the State's banks and credit co-operatives of the P.R.C., welfare benefits, survivors' pensions and relief payments, insurance indemnities, salaries of diplomatic officials of foreign embassies and consulates, and tax-free incomes as provided by international conventions to which the P.R.C. is a party or by agreements it has entered into.⁴¹³

9.4. *Real Estate Tax*

9.4.1. *The Applicable Laws*

There are two laws regulating the taxation of real estate: the 1951 Urban Real Estate Tax Regulations⁴¹⁴ and the 1986 Real Estate Tax Regulations.⁴¹⁵ Although the two laws overlap, both are currently in

411. 1987 Foreign National Income Tax Reduction Provisions, *supra* note 406, art. 2.

412. *Id.*, art. 3.

413. Individual Income Tax Law, *supra* note 345, art. 4.

414. *Chengshi Fangdi Chan Shui Zanxing Tiaoli* [Provisional Regulations Governing the Urban Real Estate Tax], promulgated by the Administration Council on Aug. 8, 1951, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 39-500 [hereinafter 1951 Urban Real Estate Tax Regulations].

415. *Fang Chan Shui Zanxing Tiaoli* [Provisional Regulations of the PRC on Real Estate Tax], issued by the State Council on Sept. 15, 1986, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 39-505 [hereinafter 1986 Real Estate Tax Regulations].

force and both are applicable to foreign investment enterprises.

9.4.2. *General Provisions*

The 1951 Urban Real Estate Tax Regulations cover all units or individuals who own real estate in urban areas. If real estate is mortgaged, the tax is to be paid by the mortgagee. In the event the owner of the estate or mortgagee is absent or there is an unsettled dispute about the property, the tax is paid by the user or custodian of the estate.⁴¹⁶

The Urban Real Estate Tax is divided into two categories, the housing property tax and the land property tax. The housing property tax is levied yearly at the rate of 1.2% of the assessed value of the building. The land property tax also is levied on a yearly basis at the rate of 1.8% of the assessed value of the land.⁴¹⁷ However, since the State itself is the owner of the land, equity joint ventures, co-operative joint ventures and wholly foreign-owned ventures are not subject to the land property tax. Instead, they are charged a "land use fee." This fee is levied only on buildings owned by the foreign investment enterprise or contributed to it by the Chinese partner. The payment for yearly real estate tax is collected once every four or six months as determined by the local tax authorities.⁴¹⁸ Similarly, under the 1986 Real Estate Tax Regulations, the owner of the property rights pays the Real Estate Tax, excluding land property tax. Where the property has been mortgaged, the Real Estate Tax is paid by the mortgagee. In case of disputes or an absence of the owner or mortgagee, the custodian or the user of the property is considered the taxpayer. The Real Estate Tax is assessed on the residual value of the original value of the property following the subtraction of 10%-30%, at the rate of 1.2%, or on the rental income from the property at the rate of 12%.⁴¹⁹

9.5. *Vehicles and Vessels Tax and Dues*

9.5.1. *The Applicable Laws*

Three sets of tax regulations are applicable to vehicles and vessels: the 1951 Vehicle and Vessel License Plate Tax Regulations,⁴²⁰ the

416. 1951 Urban Real Estate Tax Regulations, *supra* note 414, art. 3.

417. *Id.*, art. 6, note 3.

418. *Id.*, art. 8.

419. 1986 Real Estate Tax Regulations, *supra* note 415, arts. 2, 4.

420. *Che Chuan Shiyong Pai Zhao Shui Zanxing Tiaoli* [Provisional Regulations Governing the Vehicle and Vessel License Plate Tax], promulgated by the Administrative Council on Sept. 13, 1951, reprinted and translated in 3 CCH CHINA LAWS, *supra* note 18, at ¶ 34-500 [hereinafter 1951 Vehicle and Vessel License Plate Tax Regulations].

1974 Foreign Vessel Transportation Income Taxation Regulations⁴²¹ and the 1986 Vehicle and Vessel Usage Tax Regulations.⁴²²

9.5.2. General Provisions

The 1951 Vehicle and Vessel License Plate Tax Regulations provide that all drivers and operators driving or operating vehicles or vessels within specified areas are subject to the vehicle and vessel license plate tax provisions.⁴²³ The tax is normally collected once every three or six months, but collection on a yearly basis is also permissible if the local tax authorities so allow.⁴²⁴ Domestic vessels paying a tonnage tax (vessel dues) are obliged to pay a license plate tax instead of the tonnage tax. However, foreign vessels or Chinese vessels chartered by foreign firms are still required to pay the tonnage tax rather than the license plate tax.⁴²⁵

The scope, methods, tax amounts, prohibitions, and penalties of the 1951 Regulations are set out in articles 3 to 16. In particular, articles 7 and 8 set forth the license plate tax schedules for vehicles and vessels respectively. The tax rates vary from one locality to another and from one type of vehicle to another.⁴²⁶ For instance, the average tax rate for passenger vehicles is Y 160 per year while the rate for vessels is based on tonnage.⁴²⁷

The 1974 Foreign Vessel Transportation Income Taxation Regulations provide that carriers or vessels of foreign nationality carrying cargo or passengers out from a Chinese port are to pay an "industrial-commercial unified tax" and an "industrial-commercial income tax" on the gross transportation income derived from each voyage.⁴²⁸ Both taxes are to be assessed and collected together at the rate of 3% of the gross income. In addition, a local surcharge is charged at the rate of 1% of

421. Regulations for Taxation on the Transportation Income of Vessels of Foreign Nationality, enacted by the Ministry of Finance on June 21, 1974, *reprinted and translated in* 3 CCH CHINA LAWS, *supra* note 18, at ¶ 34-540 [hereinafter 1974 Foreign Vessel Transportation Income Taxation Regulations].

422. *Chechuan Shiyong Shui Zanxing Tiaoli* [Provisional Regulations of the People's Republic of China on Vehicle and Vessel Usage Tax], *issued by* the State Council on Sept. 15, 1986, *reprinted and translated in* 3 CCH CHINA LAWS, *supra* note 18, at ¶ 34-568 [hereinafter 1986 Vehicle and Vessel Usage Tax Regulations].

423. 1951 Vehicle and Vessel License Plate Tax Regulations, *supra* note 420, art. 1.

424. *Id.*, art. 5.

425. *Id.*, art. 2.

426. *See id.*, art. 6.

427. *Id.*, arts. 3-16, in particular, arts. 7, 8.

428. 1974 Foreign Vessel Transportation Income Taxation Regulations, *supra*

the amount of the above tax assessment.⁴²⁹

10. FOREIGN EXCHANGE CONTROLS AND BANKING

10.1. *The Applicable Laws*

To regulate banking, financing, and foreign exchange matters, the State Council and several other administrative organs have promulgated a new series of rules and regulations since the enactment of the 1979 Joint Venture Law. These promulgations include: the 1980 Articles of Association of the Bank of China, primarily dealing with the regulatory role of the Bank of China;⁴³⁰ the Foreign Exchange Control Regulations, the basic law on foreign exchange control governing Chinese state-owned units and collective economic entities, individuals, foreign representations and their personnel, as well as foreign investment enterprises and their personnel;⁴³¹ the 1981 Joint Venture Loan Measures, which were intended to facilitate the financing of Sino-foreign equity joint ventures;⁴³² the 1983 Foreign Currency and Renminbi Deposits Regulations, serving as the Bank of China's internal banking rules which include three separate sets of regulations: Regulations for Foreign Currency Deposits (Category A), Regulations for Foreign Currency Deposits (Category B) and Regulations for Special Renminbi Deposits;⁴³³ the 1983 Enterprise Foreign Exchange Control Rules, issued as the implementing rules of the 1980 Foreign Exchange Control Regulations with respect to foreign (including overseas Chinese) investment enterprises only;⁴³⁴ the 1985 Exchange Control Violation Rules, providing various penalties for violations of the Foreign Exchange Con-

429. *Id.*, art. 1.

430. Articles of Association of the Bank of China, *supra* note 77.

431. Foreign Exchange Control Regulations, *supra* note 55.

432. Provisional Measures of the Bank of China on the Issue of Loans to Sino-Foreign Equity Joint Ventures, *approved by* the State Council on Mar. 13, 1981, *promulgated by* the Bank of China and *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 6-530 [hereinafter 1981 Joint Venture Loan Measures] and FOREIGN ECONOMIC LEGISLATION, *supra* note 36, at 27, 32, *superseded by* the 1987 Foreign Investment Enterprise Loan Measures, *infra* note 439.

433. Regulations on Foreign Currency Deposits and Special Renminbi Deposits by the Bank of China, *promulgated and enforced by* the Head Office of the Bank of China in Jan. 1983, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-570 [hereinafter 1983 Foreign Currency and Renminbi Deposits Regulations].

434. Detailed Rules for the Implementation of Foreign Exchange Control Regulations Relating to Enterprises with Overseas Chinese Capital, Enterprises with Foreign Capital and Sino-Foreign Joint Equity Ventures, *approved by* the State Council on July 19, 1983, *promulgated by* the State Administration of Exchange Control on Aug. 1, 1983, *reprinted and translated in* 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-679, art. 1 [hereinafter 1983 Enterprise Foreign Exchange Control Rules].

trol Regulations;⁴³⁵ and the 1986 Bank Control Regulations, promulgated to tighten control over banks and other financial institutions as well as to prohibit non-financial institutions from conducting financial business.⁴³⁶ More recently promulgated are the 1986 Renminbi Loans Measures, adopted to promote the business of renminbi loans (RMB loans) mortgaged by foreign exchange;⁴³⁷ the 1987 Foreign Exchange Guarantee Measures, promulgated to promote foreign economic and technological co-operation, to ensure the smooth development of financial activities and to strengthen control over foreign exchange guarantees;⁴³⁸ and lastly, the 1987 Foreign Investment Enterprise Loan Measures, rescinding the 1981 Joint Venture Loan Measures on the date of their promulgation, promulgated to expand the scope of the latter to include "Sino-foreign equity joint venture enterprises, Sino-foreign co-operative enterprises and enterprises with sole foreign investment."⁴³⁹

10.2. General Provisions

In the P.R.C., equity joint ventures, co-operative enterprises and wholly foreign-owned enterprises are all subject to the foreign exchange control regulations and rules of the People's Republic of China.⁴⁴⁰ The Joint Venture Law and the Joint Venture Law Implementation Regu-

435. *Weifan Wai Hui Guanli Chufa Shixing Xize* [Detailed Implementation Rules and Regulations Governing Violation of Exchange Control of the People's Republic of China], approved by the State Council on Mar. 25, 1985, promulgated by the State Administration of Exchange Control on Apr. 5, 1985, reprinted and translated in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-675, arts. 3, 5, 7, 8, 9 [hereinafter 1985 Exchange Control Violation Rules].

436. *Yinhang Guanli Zanxing Tiaoli* [Provisional Regulations of the People's Republic of China on the Control of Banks], promulgated by the State Council on Jan. 7, 1986, reprinted and translated in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-690 [hereinafter 1986 Bank Control Regulations].

437. *Wai Shang Touzi Qiye Wai Hui Diya Renminbi Daikuan Zanxing Banfa* [Provisional Measures of the People's Republic of China on Foreign Exchange Secured Renminbi Loans for Foreign Investment Enterprises], art. 1, promulgated by the People's Bank of China on Nov. 26, 1986, reprinted and translated in 1 CCH CHINA LAWS, *supra* note 24, at ¶ 8-694, [hereinafter 1986 Renminbi Loans Measures].

438. *Jingnei Jigou Tigong Wai Hui Danbao De Zanxing Guanli Banfa* [Provisional Measures for the Control of the Issue of Foreign Exchange Guarantees by Organizations within Chinese Territory], promulgated by the People's Bank of China on Feb. 20, 1987, reprinted and translated in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-698 [hereinafter 1987 Foreign Exchange Guarantee Measures].

439. *Dui Wai Shang Touzi Qiye Daikuan Banfa* [Measures of the Bank of China on Loans for Foreign Investment Enterprises] approved by the State Council on Apr. 7, 1987, promulgated by the Bank of China on Apr. 24, 1987, reprinted and translated in 1 CCH CHINA LAWS, *supra* note 18, at ¶ 8-702, arts. 3, 27 [hereinafter 1987 Foreign Investment Enterprise Loan Measures]. It may be noted that the 1987 Measures were unofficially implemented in 1986. See *The Bank of China Amended Its Foreign Investment Enterprise Loans Measures*, People's Daily, Oct. 31, 1986, at 3.

440. See *Foreign Exchange Control Regulations*, *supra* note 55, ch. V.

lations provide that all matters of a joint venture concerning foreign exchange are to be handled in accordance with the foreign exchange control regulations and other relevant control measures. In order to facilitate their regulation, joint ventures must open their foreign currency deposit accounts and RMB deposit accounts with the Bank of China or another approved bank.⁴⁴¹

An early draft of the Wholly Foreign-Owned Enterprise Law did not contain any provision concerning foreign exchange matters in a wholly foreign-owned enterprise. After lengthy discussions in legislative, academic and foreign business circles, it was concluded that foreign investors were concerned with balancing foreign exchange receipts against expenditures, and that basic guidelines should be provided to achieve this end.⁴⁴² Upon recommendations submitted by the Legal Committee of the N.P.C., two articles were added to the final draft of the Wholly Foreign-Owned Enterprise Law providing that a) wholly foreign-owned enterprises are subject to State regulations governing foreign exchange control, b) any problems concerning the balance of foreign exchange should be independently resolved by the wholly foreign-owned enterprise,⁴⁴³ and c) legitimate profits earned, as well as legitimate income and funds obtained after liquidation of the enterprise by the foreign owner may be remitted out of the P.R.C.⁴⁴⁴ Foreign personnel working in wholly foreign-owned enterprises may also remit their wages and other legitimate income outside the P.R.C. after paying individual income tax.⁴⁴⁵ Lastly, for co-operative development projects in coal, oil and other natural resources whose profit is shared by way of output distributions, special rules allow the free remittance of the por-

441. Joint Venture Law, *supra* note 36, art. 8; Joint Venture Law Implementation Regulations, *supra* note 52, arts. 73, 74.

442. *Report on the Result of Examination and Discussion of the Solely Foreign-Invested Enterprise Law Draft*, People's Daily, Mar. 12, 1986, at 3.

443. Wholly Foreign-Owned Enterprise Law, *supra* note 37, art. 18. Art. 18 reads as follows:

Matters relating to the foreign exchange of an enterprise with sole foreign investment shall be handled in accordance with the State regulations governing foreign exchange control.

An enterprise with sole foreign investment shall open a bank account with the Bank of China or a bank designated by the State General Administration of Foreign Exchange Control. An enterprise with sole foreign investment shall itself resolve its balance of foreign exchange income and expenditure. Where the products of an enterprise with sole foreign investment are sold, with the approval of the competent authorities, on the Chinese domestic market and it results in the creation of an imbalance in foreign exchange income and expenditure, the body which approved such domestic sales shall be responsible for resolving the imbalance.

444. *Id.*, art. 19.

445. *Id.*

tion of output earned by the foreign partner.⁴⁴⁶

Under the Foreign Exchange Control Regulations, all receipts of a foreign investment enterprise in foreign currencies must be deposited in the Bank of China or another approved bank unless otherwise stipulated by Chinese law. All foreign exchange expenditure payments must be made out of their foreign exchange deposit accounts.⁴⁴⁷ Payments to domestic enterprises or to individuals in the P.R.C. must be made out of their RMB deposit accounts unless approval is received from the SAEC or one of its local branches.⁴⁴⁸ The remittance of net profits after tax payments, and payment settlement upon the enterprise's legal termination, must be made out of their foreign exchange deposit accounts.⁴⁴⁹

The 1983 Enterprise Foreign Exchange Control Rules permit foreign investors to keep foreign exchange earnings in foreign bank accounts if a satisfactory method of assuring the payment of the venture's operation costs is approved by the foreign exchange control authorities.⁴⁵⁰ Foreign partners involved with a co-operative exploitation of the P.R.C.'s offshore petroleum resources may deposit their exploration fund and their co-operatively provided development and production funds in foreign banks agreed upon by the Chinese partner; no approval from the SAEC or a branch thereof is necessary.⁴⁵¹

A foreign investment enterprise may raise funds directly from a bank or enterprise located outside the P.R.C.,⁴⁵² provided that it report such fund-raising activities to the SAEC or its branch offices.⁴⁵³ It may also apply to the Bank of China for foreign exchange loans and RMB loans if it satisfies certain conditions.⁴⁵⁴ The Bank of China is the

446. See, e.g., The 1982 Offshore Petroleum Regulations, *supra* note 140, arts. 7, 8, and *supra* notes 143-48 and accompanying text.

447. Foreign Exchange Control Regulations, *supra* note 55, art. 22; Joint Venture Law Implementation Regulations, *supra* note 52, art. 74. See Foreign Exchange Control Regulations, art. 4.

448. Foreign Exchange Control Regulations, *supra* note 55, art. 23.

449. *Id.*, arts. 24, 26.

450. 1983 Enterprise Foreign Exchange Control Rules, *supra* note 434, art. 6. See also Joint Venture Law Implementation Regulations, *supra* note 52, art. 76 ("A joint venture shall get permission from the State General Administration of Foreign Exchange Control or one of its branches to open a foreign exchange deposit account with an overseas bank or one in Hong Kong or Macao, and report to the State General Administration of Foreign Exchange Control or one of its branches its foreign exchange receipts and expenditures and provide account sheets").

451. 1983 Enterprise Foreign Exchange Control Rules, *supra* note 434, art. 5.

452. Joint Venture Law, *supra* note 36, art. 8; 1983 Enterprise Foreign Exchange Control Rules, *supra* note 434, art. 17.

453. Joint Venture Law Implementation Regulations, *supra* note 52, art. 78;

1983 Enterprise Foreign Exchange Control Rules, *supra* note 434, art. 17.

454. 1987 Foreign Investment Enterprise Loan Measures, *supra* note 439, arts.

State's specialized foreign exchange bank, and is empowered to engage in various loan transactions, to issue foreign currency bonds and other securities and to engage in other banking and financing activities.⁴⁵⁵

11. DISPUTE SETTLEMENT

The Chinese people have traditionally been reluctant to settle disputes in courts or even before arbitration tribunals. Friendly negotiations (consultations) and conciliations (mediation) have been the preferred routes. This preference for informal dispute resolution still exists today in both legislative and contractual disputes. Arbitration clauses in the P.R.C. are commonly prefaced with a plea for friendly negotiations before resorting to arbitration.⁴⁵⁶ Most cases settle and rarely advance to litigation or even arbitration. This is demonstrated in the Joint Venture Law, the Joint Venture Law Implementation Regulations and the Shenzhen Foreign Economic Contract Regulations.⁴⁵⁷ The Joint Venture Law contains language such as "consultation" and "conciliation," two mechanisms which are clearly preferred over arbitration.⁴⁵⁸ It is interesting to note, however, that the 1985 Foreign Economic Contract Law does not contain similar language. Instead, Article 37 of that law allows the parties to a foreign economic contractual agreement to select an appropriate method of settlement although they are strongly encouraged to settle disputes through informal mechanisms.⁴⁵⁹ Thus the contracting parties are under no legal obligation to invoke informal mechanisms for dispute resolution.

3, 7; Joint Venture Law Implementation Regulations, *supra* note 52, art. 78.

455. Articles of Association of the Bank of China, *supra* note 77, arts. 1, 2, 5.

456. See, e.g., United States-People's Republic of China Agreement on Trade Relations, *supra* note 57, art. VIII:

1. The Contracting Parties encourage the prompt and equitable settlement of any disputes. . . . through friendly consultations, conciliation or other mutually acceptable means.

2. If such disputes cannot be settled promptly by any of the above-mentioned means, the parties to the dispute may have recourse to arbitration

457. Joint Venture Law, *supra* note 36, art. 14; Joint Venture Law Implementation Regulations, *supra* note 52, art. 109; Regulations of Shenzhen Special Economic Zone on Economic Contracts Involving Foreigners, *approved by* the Standing Committee of the Sixth Guangdong Provincial People's Congress on Jan. 11, 1984, *promulgated by* the Guangdong Provincial People's Government on Feb. 7, 1984, *reprinted in* 3 CCH CHINA LAWS, *supra* note 18, at ¶ 73-505, art. 34 [hereinafter Shenzhen Foreign Economic Contract Regulations].

458. Joint Venture Law, *supra* note 36, art. 14. Article 14 provides that the parties who "[fail] to settle through consultation" disputes arising between them may settle the same "through conciliation or arbitration by an arbitral body of China or through arbitration by an arbitral body agreed upon by [them]."

459. Foreign Economic Contract Law, *supra* note 42, art. 37.

Similarly, the Co-Operative Enterprise Law cast away the language contained in the Joint Venture Law that makes resort to consultations and mediation first obligatory. Although Article 26 of the Co-Operative Enterprise Law indicates that "a dispute . . . shall be resolved through consultation or mediation," it also points out that "[i]f the Chinese and foreign partners are unwilling to use consultation or mediation to resolve the dispute," the matter may be submitted to a Chinese or other arbitral body for arbitration if there is an arbitration agreement between the parties.⁴⁶⁰ Under the law, a dispute may also be submitted to a Chinese court where there is no arbitration clause or agreement.⁴⁶¹

Chinese arbitration organizations do not assume exclusive jurisdiction over disputes arising within a joint venture. The Joint Venture Law permit parties to a joint venture to select between Chinese and foreign arbitral bodies.⁴⁶²

The Chinese party to a joint venture generally prefers arbitration to take place within the P.R.C. The CCPIT, through its Foreign Economic and Trade Arbitration Commission (FETAC), serves as a general Chinese arbitral body which provides services in foreign commercial dispute settlement. The Arbitration Rules were formulated and issued in 1956 to govern the operation of the Foreign Trade Arbitration Commission (FTAC), which was created in 1954.⁴⁶³ In 1980, the State Council converted the former FTAC to the present FETAC in order to enlarge its scope of dispute resolution "to [an] extent that covers the disputes arising from various kinds of China's economic cooperation with foreign countries such as joint ventures using Chinese and foreign investment[s], foreign investment[s] to build factories in China, [etc.]."⁴⁶⁴ This semi-official arbitral body settles disputes according to the principles of independence and of equality and mutual benefit with regard to international practice by strictly obeying Chinese laws and observing contractual provisions. Before arbitration begins, the plaintiff must deposit 0.5% of the amount of the claim, together with the claim

460. Co-Operative Enterprise Law, *supra* note 38, art. 26(1).

461. *Id.*, art. 26(2).

462. Joint Venture Law, *supra* note 36, art. 14.

463. *Zhongcai Chengxu Zanxing Guize* [Provisional Rules of Procedure of the Foreign Trade Arbitration Commission of the China Council for the Promotion of International Trade], *adopted* by the Fourth Session of the China Council for the Promotion of International Trade on March 31, 1986, *reprinted and translated* in 2 CCH CHINA LAWS, *supra* note 18, at ¶ 10-500 [hereinafter 1986 Arbitration Rules].

464. State Council's Notice Concerning the Conversion of Foreign Trade Arbitration Commission into Foreign Economic and Trade Arbitration Commission (issued on Feb. 26, 1980), *reprinted and translated* in CHINA IMPORT-EXPORT GUIDE,

application, to the FETAC.⁴⁶⁵ The decisions of the FETAC once rendered, can not be appealed.⁴⁶⁶

The Chinese have recently begun to encourage foreign arbitrations and foreign arbitration rules. The preferred — or those considered by the Chinese to be the most “neutral” — arbitral bodies are the Arbitration Institute of the Stockholm Chamber of Commerce, the London Court of Arbitration, the Zurich Chamber of Commerce in Switzerland and the Hong Kong International Arbitration Centre. A fifth arbitral body, the International Chamber of Commerce in Paris has not yet been invoked because of the Taiwan authorities’ illegal representation therein.⁴⁶⁷ As a result, the 1976 UNCITRAL Arbitration Rules are often chosen as the governing rules by the selected arbitral body.⁴⁶⁸ Recently, the P.R.C. has also acceded to the 1958 U.N. Convention on the Recognition and Enforcement of Foreign Arbitral Awards.⁴⁶⁹ Additionally, enforcement of foreign arbitral awards in the P.R.C. may be sought under the provisions of the 1982 Trial Civil Procedure Code. Article 204 of that Code provides that foreign arbitral awards must have initially been converted into a foreign judgment and then entrusted to Chinese courts for enforcement, and that foreign judgments will not be executed by a Chinese court if they violate basic principles of Chinese laws and the P.R.C.’s national interests. However, it is unclear from the Code what necessary steps must be taken in order to obtain enforcement from Chinese courts. Moreover, converting the award to a foreign judgment may in certain instances be a burdensome requirement for a foreign country. It is often difficult to judge whether the requirement of not having violated Chinese law and national policy is met. These difficulties may be minimized by the P.R.C.’s accession to

465. 1986 Arbitration Rules, *supra* note 463, art. 31.

466. *Id.*, art. 6.

467. See Zheng, *A Comparative Analysis of the Foreign Economic Contract Law of the People's Republic of China*, 3 CHINA L. REP. 227, 255 n.145 (1986).

468. See Cohen, *The Role of Arbitration in Economic Co-operation with China*, in FOREIGN TRADE, INVESTMENT, AND THE LAW IN THE P.R.C., *supra* note 70, 508, at 521.

469. U.N. Convention on the Recognition and the Enforcement of Foreign Arbitral Awards (New York Convention), *opened for signature* 1959, 21 U.S.T. 2517, T.I.A.S. No. 6997, 330 U.N.T.S. 38. The Eighteenth Session of the N.P.C. decided, on December 2, 1986, to accede to the New York Convention. See *People's Daily*, Dec. 3, 1986, at 1. With respect to the P.R.C. the convention came into effect ninety(90) days after the P.R.C.’s official accession with the U.N. Secretariat, which occurred on January 22, 1987. Thus, as of April 22, 1987, China has been bound, by the New York Convention, to enforce arbitration awards rendered in other contracting countries in Chinese courts. The P.R.C. has made a reservation, however, that it will only recognize and enforce arbitration awards rendered in another contracting country *on the basis of reciprocity*, and that the P.R.C. will abide by the Convention on the condition that such disputes must have involved commercial matters as determined by Chinese law. *Id.*

the New York Convention, and by existing bilateral agreements on foreign award enforcement between the P.R.C. and other countries. The P.R.C. has concluded bilateral agreements with the United States, Sweden and Japan. Finally, although judicial proceedings are the least favored mechanism for dispute resolution, parties may, in the absence of an arbitration clause, resort to judicial litigations in Chinese courts.⁴⁷⁰

It is recommended that the parties to foreign investment enterprises should establish clear dispute resolution procedures specifying, among other things, the arbitral body, place and governing law in the joint venture or co-operation contract. This would more effectively secure both parties' position in the joint venture or co-operative enterprise, and may avoid the need to institute litigation and/or arbitration.⁴⁷¹

12. CONCLUSION

The People's Republic of China has been very successful in attracting foreign investment and technology during the last decade. The overall environment for foreign investment in the P.R.C. has significantly improved during the same period. While the existing laws and regulations do not provide a comprehensive framework whereby a foreign investor can be 100% certain of how his or her investment should be structured and would be treated, the Chinese Government has developed reasonable and flexible investment requirements that provide basic guidance, structure and precedence. New forms of foreign investment, most notably the wholly foreign-owned enterprise, provide flexibility and greater opportunities for foreign investors. The tax incentives and other preferential treatments available to foreign investors are significant. The legislative framework for foreign investment is becoming increasingly comprehensive. The P.R.C. has become a more active participant in international conventions and agreements, and where accession is pending, it has been faithfully following established inter-

470. Trial Civil Procedure Code, *supra* note 40, art. 204.

471. Foreign Economic Contract Law, *supra* note 42, art. 37. See also, Joint Venture Law Implementation Regulations, *supra* note 52, art. 111; Co-Operative Enterprise Law, *supra* note 38, art. 26.

For a more in-depth discussion of dispute resolution in China, see generally Cohen, *supra* note 468; Ingriselli, *International Dispute Resolution and the People's Republic of China*, 12 INT'L BUS. LAW. 376 (1984); Klitgaard, *People's Republic of China Joint Venture Dispute Resolution Procedures*, 1 UCLA PAC. BASIN. L. J. 1 (1982); Pettit, *Dispute Resolution in the People's Republic of China*, 39 ARB. J. 3 (1984); Potter, *Resolving Contract Disputes*, CHINA BUS. REV., Sept.-Oct. 1984, at 21; Surrey, *Dispute Settlement in U.S.-China Trade — Another Look*, in LEGAL ASPECTS OF DOING BUSINESS IN CHINA 277 (Practicing Law Institute Commercial Law and Practice Course Handbook Series No. 349, 1985).

national practice. The Chinese people and their leaders sincerely desire to continue the open-door policy, ongoing reform, and co-operation with foreign businessmen. More favorable conditions have been created in the areas of taxation, technology transfer, foreign exchange regulation, and dispute resolution as well as other matters. Thus, despite existing problems such as the lack of comprehensive legislation, the uncertainty of various legal provisions, the long-lasting bureaucracy, and the shortage of foreign exchange, the basic legal framework for foreign investment in the P.R.C. is on sound footing, and should bolster the confidence of present and future foreign investors.